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IN THE
Supreme Court of the United States

GEORGIA-PACIFIC CORPORATION
SALARIED EMPLOYEES RETIREMENT PLAN AND
GEORGIA-PACIFIC CORPORATION,
Petitioners,

v.

JERRY L. LYONS, individually and on
behalf of all other persons similarly situated,
Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Eleventh Circuit

PETITION FOR A WRIT OF CERTIORARI

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QUESTIONS PRESENTED

During the past decade, numerous employers have adopted employee defined benefit plans under the Employee Retirement Income Security Act ("ERISA") commonly referred to as "cash balance" plans. These plans have become popular because they provide unique financial benefits to employees and employers. The important issue that has arisen under ERISA regarding these plans is how to calculate the amount to which an employee is entitled in the event he or she retires early. The court of appeals in this case rejected the straightforward approach adopted by the plan administrator of distributing precisely the amount then held in the plan for the benefit of that employee. The questions presented to this Court by that holding are:

1. Whether ERISA denies "cash balance" plans the freedom to pay a departing employee who elects to receive a "lump sum" benefit an amount equal to the employee's account balance as expressly provided by the plan, or whether it requires instead that the plan pay the employee an amount based on a "projecting forward/discounting backward" formula.

2. Whether the court of appeals' decision that favorable IRS determination letters and an IRS "safe harbor" provision relate only to "tax qualification" subjects plan sponsors to inconsistent obligations under ERISA and the parallel provisions of the Tax Code in violation of ERISA § 3002(c) (29 U.S.C. § 1202(c)) and Reorganization Plan No. 4 of 1978, 92 Stat. 3790.

3. Whether applying the IRS's "projecting forward/ discounting backward" formula to voluntary distributions under Petitioners' "cash balance" plan violates the fair notice doctrine.

PARTIES TO THE PROCEEDING

All parties to the proceeding are listed in the caption of the case. Georgia-Pacific Corporation does not have a parent company. Two publicly traded funds, Longleaf Partners Fund and The Income Fund of America, Inc., own a beneficial interest of more than 10 percent of a class of Georgia-Pacific tracking stock (The Timber Group Company (NYSE: TGP)). See Sup. Ct. R. 29.6.

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PETITION FOR A WRIT OF CERTIORARI

Petitioners, Georgia-Pacific Corporation Salaried Employees Retirement Plan and Georgia-Pacific Corporation, respectfully petition for a writ of certiorari to review the judgment of the United States Court of Appeals for the Eleventh Circuit in this case.

OPINIONS BELOW

The opinion of the court of appeals (App. 1a-37a) was entered on August 11, 2000, and is reported at 221 F.3d 1235 (11th Cir. 2000). The order denying the petition for rehearing and rehearing *en banc* (App. 54a) was entered on October 25, 2000, and is not reported. The opinion of the United States District Court for the Northern District of Georgia (App. 38a-

53a) was entered on March 22, 1999, and is reported at 66 F.Supp.2d 1328 (N.D.Ga. 1999).

JURISDICTION

The court of appeals entered its decision and judgment on August 11, 2000. Petitioners timely filed a petition for rehearing and a suggestion for rehearing *en banc* on September 1, 2000, and the Petition was denied on October 25, 2000. This Court has jurisdiction pursuant to 28 U.S.C. § 1254(1).

STATUTES AND REGULATIONS INVOLVED

The primary statute involved is § 203(e) of the Employee Retirement Income Security Act of 1974 ("ERISA"), 29 U.S.C. § 1053(e) (App. 55a-56a), and the primary regulations involved are Treas. Reg. §§ 1.411(a)-11 and 1.417(e)-1(d) (App. 56a and 56a-59a, respectively).[1]

INTRODUCTION

This case presents important federal questions involving a relatively new, and yet widely adopted, form of ERISA pension plan called a "cash balance" plan. Cash balance plans are employer-sponsored pension plans that establish bookkeeping accounts for each employee to reflect the value of the employee's retirement benefit. Since their introduction roughly 15 years ago, cash balance plans have been adopted by a large number of employers and consequently affect a significant number of employees.[2] The primary issue in this

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[1] IRC §§ 411 and 417 are parallel sections of the Tax Code to ERISA § 203(e). Section 3002 of ERISA provides that Treasury Regulations promulgated under IRC § 411 apply to ERISA § 203(e). 29 U.S.C. § 1202(c).

[2] For example, a February 2000 article cited in the Eleventh Circuit's opinion claims that cash balance plans have been adopted by more than

case is whether cash balance plans can be subjected to a phenomenon called "whipsaw" that requires plan sponsors to pay amounts far greater than the employees' stated account balances.

The decision of the Eleventh Circuit in this case, and that of the Second Circuit in a similar case, *Esden* v. *Bank of Boston*, 229 F.3d 154 (2d Cir. 2000), expose employers who offer cash balance plans to substantial and unanticipated liability. Unless this Court reviews the holding below, Petitioners and similarly situated plan sponsors may be obligated to pay hundreds of millions of dollars more than expressly provided in the plans they sponsored – and departing employees will receive an unjustified windfall.

The court of appeals held that rather than paying an employee who opts for a lump sum benefit prior to retirement a benefit equal to his current account balance (the amount expected by the employee and funded by the employer), a cash balance plan must instead project the employee's retirement benefit *forward* to retirement age using the plan's interest crediting rate, and then discount the value of the benefit *back* to the present using a lower interest rate specified in a Treasury Department regulation.[3] As the district court observed, this "computational contrivance," which has the effect of paying employees a benefit for years in which they neither worked for the employer nor participated in the plan, "has only slight connection with economic reality" (App. 52a) and "do[es] not so much preserve benefit as [it] create[s] an economic windfall not intended by ERISA." *Id.* at 53a. This undermines settled

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300 employers and involve hundreds of billions of dollars in pension assets. *See* App. 3a n.2 (citing *Q-and-A: What You Need to Know About Today's "Cash-Balance" Plans*, Payroll Manager's Report, Feb. 2000, at 3).

[3] This is commonly referred to as "whipsaw" to capture the idea of jerking the calculation forward and then back.

expectations, contrary to the purposes of ERISA, and, more fundamentally, threatens the ability of employers and employees to design their own pension plan alternatives to meet the needs of a changing labor force.

The court of appeals also dismissed specific IRS determination letters that verified the Plan's compliance with the relevant provisions of law. This is not only improper and unfair, but it also gives rise to inconsistent standards of conduct for ERISA plan sponsors under the parallel provisions of ERISA and the Tax Code.

Finally, the court of appeals violated the fair notice doctrine by subjecting the Plan to whipsaw, even though the IRS first suggested this "requirement" only in a tentative, prospective notice, I.R.S. Notice 96-8, 1996-1 C.B. 359 (App. 60a–72a), issued three years *after* Respondent requested and received his lump sum distribution.

By any measure, Petitioners' distribution to Respondent conformed with a reasonable, good faith interpretation of existing law. Neither ERISA nor the Treasury Regulations require cash balance plans to apply a "project forward/discount backward" formula.

Guidance by this Court is necessary to clarify the freedom of employers to design cash balance plans with the flexibility and transparency desired by the modern work force, to maintain the parallel structure intended by Congress between the requirements of ERISA and the Tax Code, and to clarify that regulatory interpretations may not be imposed on private parties without providing fair notice of how the supposed obligations would apply to them.

STATEMENT OF THE CASE

Background

Historically, ERISA has recognized two kinds of pension plans: "defined benefit" plans, in which an employee

typically receives a lifelong annuity starting at retirement age, and "defined contribution" plans, in which employees have their own accounts that vary with investment performance (*e.g.*, a 401(k) plan). See 29 U.S.C. § 1002(34), (35). The ERISA pension plan at issue in this case is a hybrid form of defined benefit plan called a "cash balance" plan. These plans are called cash balance plans because a bookkeeping account is set up for each employee that expresses the accumulated value of contributions made by the employer on the employee's behalf and interest credits at a rate specified in the plan. Thus, the employee's retirement benefit is expressed as a single sum (*i.e.*, a "cash balance").

Under a traditional, defined benefit plan, the retirement benefit is expressed as an annuity starting at a specified retirement age, usually between 55 and 65. The value of that annuity is typically based on a formula tied to years of service and annual salary before retirement. If a traditional defined benefit plan allows employees leaving before retirement to take a lump sum benefit in lieu of an annuity (many plans do not), the present value of the employee's benefit cannot be calculated without using a mortality table and a discount rate.

With a cash balance plan, however, as with defined contribution plans such as 401(k) plans, there is no need to use mortality tables or discount rates to calculate present value. The present value of the benefit *is* the current account balance, which fully reflects all contributions to the account to-date, plus any investment returns and accumulated interest. Cash balance plans offer several advantages over more traditional plans. First, they are designed to meet the needs of a modern, increasingly mobile workforce because a greater proportion of benefits accumulate earlier in a worker's career and the benefits are more portable. See Senate Comm. on Fin., June 30, 1999 (statement of Patrick J. Purcell), *reprinted in* 1999 WL 20009611. For this reason, cash balance plans particularly benefit workers who change jobs throughout their careers and women, who are more likely to leave their jobs

for periods of time in mid-career. See Carol Quick, *Notes: An Overview of Cash Balance Plans* (Employee Benefit Research Institute) July 1999, at 7. Second, because the total assets of the Plan are pooled, the employer bears the investment risk, rather than the employees. Third, cash balance plans spread out pension costs over an employee's entire career, so that employers are not faced with rapidly escalating costs as workers approach retirement. *Id.*

The cash balance plan at issue in this case reflected these features. The Plan provided periodic pay credits to each employee's account equal to a stated percentage of the employee's pay. These amounts were further credited with an interest rate specified in the Plan until the accounts were distributed. The value of the plan accounts was periodically communicated to participating employees, including the Respondent.

Because cash balance plans combine elements of both traditional defined benefit plans and defined contribution plans, they do not fit well into the regulatory framework designed to govern more traditional plans. See Senate Comm. on Fin., *supra.* While they are "defined benefit" plans for purposes of ERISA, see ERISA § 3(35), 29 U.S.C. § 1002(35), many of the statutory and regulatory provisions designed for such plans are irrelevant to cash balance plans.

Statutory and Regulatory Provisions

The primary statutory provision at issue in this case, ERISA § 203(e), 29 U.S.C. § 1053(e), was added to ERISA as part of the Retirement Equity Act of 1984, Pub. L. No. 98-397, sec. 105(a), § 1053, 98 Stat. 1426, 1436. As part of the Tax Reform Act of 1986, Pub. L. No. 99-514, sec. 1139(c)(1), § 1053(e)(2), 100 Stat. 2085, 2487-88, Congress amended § 203(e)(2) so that § 203(e)(1)-(2) read as follows:

(e) Restrictions on mandatory distributions

(1) If the present value of any nonforfeitable benefit with respect to the participant in a plan exceeds $3,500, the plan shall provide that such benefit may not be immediately distributed without the consent of the participant.

(2)(A) *For purposes of paragraph (1) the present value shall be calculated* – (i) by using an interest rate no greater than the applicable interest rate if the vested accrued benefit (using such rate) is not in excess of $25,000, and (ii) by using an interest rate no greater than 120 percent of the applicable interest rate if the vested accrued benefit exceeds $25,000 (as determined under clause (i)). In no event shall the present value determined under subclause (II) be less than $25,000.

(B) Applicable interest rate. – For purposes of subparagraph (A), the term "applicable interest rate" means the interest rate which would be used (as of the date of the distribution) by the Pension Benefit Guarantee Corporation for purposes of determining the present value of a lump sum distribution on plan termination.

(Emphasis added.)

In 1994, following the distribution to Respondent, ERISA § 203(e)(2) was amended again as part of the Retirement Protection Act. 29 U.S.C. § 1053(e)(2) (2000).

Two Treasury Regulations promulgated in 1988 are at issue in this case. The first, Treasury Regulation § 1.411(a)-11, interprets IRC § 411.[4] See 53 Fed. Reg. 31837, 31853 (Aug. 22, 1988). In 1993, when Respondent received his distribution, that regulation stated that IRC § 411(a)-11:

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[4] IRC §§ 411 and 417 are parallel sections of the Tax Code to ERISA § 203(e). *See* n.1, *supra.*

> [R]estricts the ability of defined benefit plans to distribute any portion of a participant's accrued benefit in optional forms of benefit without complying with specified valuation rules for determining the amount of the distribution. If the consent requirements or the valuation rules of the section are not satisfied, the plan fails to satisfy the requirements of section 411(a).

Treas. Reg. § 1.411(a)-11(a)(1) (1988).

Section 1.417(e)-1(d) (1988), in turn, applies the "valuation rules" specified in IRC § 417(e):

> For purposes of determining the present value of any accrued benefit and for purposes of determining the amount . . . of any distribution including a single sum, a defined benefit plan is subject to [specified interest rate limitations]. The present value of any optional form of benefit cannot be less than the present value of the normal retirement benefit determined in accordance with this paragraph.

Id. § 1.417(e)-1(d) (1988). Neither these regulations, nor their preambles, specifically address cash balance plans. See 53 Fed. Reg. 31837.

IRS Materials

In 1996, for the first time, the IRS expressed its tentative view that cash balance plans are required to project interest rates forward and discount them back to present value.[5] The agency also implied, for the first time, that cash balance plans might, in the future, be required to use standard interest crediting rates. See I.R.S. Notice 96-8 (App. 60a-72a).

The "Purpose" section of the Notice explains that "[t]he proposed guidance is being described in this notice in order *to permit advance public comment in anticipation of regulations*

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[5] Petitioners are not aware of any whipsaw claims asserted against cash balance plans prior to the issuance of Notice 96-8.

that incorporate the proposed guidance." App. 60a (emphasis added). The Notice states the IRS's belief that compliance with IRC §§ 411(a) and 417(e) requires cash balance plans to project the employee's account balance forward to normal retirement age and then discount it back to determine the present value of lump sum distributions. The Notice also contains a safe harbor provision:

> [F]or plan years beginning before the regulations are effective, a frontloaded interest credit plan would not be disqualified for failing to satisfy section 411(a) or 417(e) if the amount of the distribution satisfied those sections based on a reasonable, good-faith interpretation of the applicable provisions of the Code, taking into account preexisting guidance.

Id. at 71a. To date, the regulations contemplated by Notice 96-8 have not been promulgated, and the "proposed guidance" for cash balance plans – which was issued in 1996 merely "to permit advance public comment" – has never been finalized.

IRS determination letters are also crucial to this case. The IRS issues such letters to pension plans to approve the plans as "tax qualified" (and thus entitled to favorable tax treatment). Before the IRS will issue a determination letter, it must verify that the plan complies with clearly established Treasury Regulations, Treas. Reg. § 601.201(a)(3), including the interest rate limitations of IRC § 417(e) (which are the same as ERISA § 203(e)). See Worksheet Number 2A – Determination of Qualification (Department of the Treasury – Internal Revenue Service) 2000, at V.g. (App. 77a). In 1989, before Respondent received his distribution, the Plan requested and received a favorable determination letter. App. 86a-88a. In 1997, the Plan requested and received a second favorable determination letter. *Id.* at 89a-91a.

Case History

Respondent Jerry L. Lyons, a Plan participant, voluntarily retired from Georgia-Pacific on January 5, 1991. In November 1992, he opted to receive his benefit in the form of a lump sum payment under § 6.4(C). In January 1993, he was paid his current account balance, or $36,109.15. There is no dispute that the lump sum paid by the Plan was the amount properly credited to his account and the amount he expected to receive under the terms of the Plan.

Approximately three years later, in March 1996, Respondent asserted (through the National Center for Retirement Benefits)[6] that he was entitled to $49,341.83, or roughly $13,000 more than his account balance when he elected to receive a lump sum payment. Respondent claimed that Treasury Regulation § 1.417(e)-1 mandates that the amount of a lump sum payment be no less than the "present value" of his normal retirement benefit (an annuity starting at age 65) which would include interest credits projected forward until age 65. Consequently, he argued, the regulation entitled him to more than the $36,109.15 paid to him under the terms of the Plan.

In response, the administrator of the Plan determined that Respondent's lump sum distribution was proper, because the Plan did not provide for account balances to be projected forward and then discounted back. See App. 82a-85a. The administrator stated that cash balance plans are a special form of defined benefit plan that, consistent with IRS Notice 96-8, define benefits for each employee with reference to the employee's account balance. *Id.* at 83a.

On April 14, 1997, Respondent filed suit in the United States District Court for the Northern District of Georgia, individually, and on behalf of all others similarly situated.

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[6] The NCRB is a for-profit company that specializes in identifying alleged errors in pension benefit calculations.

Respondent claimed that the payment of a lump sum benefit equal to his account balance violated ERISA and various Treasury Regulations because the account balance was less than the "present value" of his retirement benefit.

The complaint alleged that Treasury Regulations §§ 1.411(a)-11 and 1.417(e)-1 required his account balance to be credited with interest to "Normal Retirement Age" (age 65) using the Plan's interest crediting rate for amounts left in the Plan, and then discounted to present value at a rate specified by the Pension Benefit Guaranty Corporation (the "PBGC rate"). Respondent claimed that, when projected to age 65, the difference between the higher interest crediting rate and the lower discount rate yielded a lump sum payout of $49,341.83, or approximately $13,000 more than his account balance.[7]

The parties stipulated to a class of all participants in the Plan who received a lump sum benefit that was lower than the "present value, if determined using the 'applicable interest rate'" as defined in the Internal Revenue Code and related regulations. App. 40a. The court also entered a consent order permitting the parties to submit cross motions for summary judgment on the threshold issue of liability before engaging in discovery and proceedings relating to the claims and/or defenses as to each class member. *Id.*

The district court granted summary judgment in favor of the Plan, holding that the Treasury Regulations §§ 1.411(a)-11 and 1.417(e)-1(d) exceeded the scope of ERISA § 203(e) and were therefore unenforceable. App. 51a-53a. Noting that

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[7] Although the parties agree that Respondent was entitled to $36,109.15 *under the terms of the Plan* (Respondent conceded as much in the Complaint, *see* Compl. ¶ 28), the parties dispute what lump sum Respondent should have received if the projection forward/discount back formula applied (*i.e.*, even if the projection forward/discount back formula applied, Petitioners dispute that Respondent would be entitled to $49,341.83).

Respondent freely elected to take the lump sum distribution, the district court explained that the higher benefit claimed under the Treasury Regulations arose only as a result of a "computational contrivance that has only slight connection with economic reality." *Id.* at 52a. The court concluded that the regulations "do not so much preserve benefit value as they create an economic windfall not intended by ERISA." *Id.* at 53a.

Respondent filed a timely appeal with the Eleventh Circuit. On August 11, 2000, that court reversed and remanded the case to the district court for further proceedings. App. 37a. Relying on *Chevron U.S.A. Inc.* v. *Natural Resources Defense Council, Inc.*, 467 U.S. 837, 843 (1984), the court concluded that ERISA § 203(e) and its legislative history were ambiguous (App. 18a-22a) and that Treasury Regulation § 1.411(a)-11 constituted a reasonable interpretation of that statute. *Id.* at 24a-26a.

The court rejected Petitioners' argument that the regulations were invalid and that, even if valid, they did not apply to cash balance plans. The court recognized that Notice 96-8 could not be determinative, because it was issued after Respondent requested and received his benefit (App. 28a), but nonetheless concluded that Petitioners had sufficient notice of the project forward/discount backward valuation requirement. *Id.* at 28a-30a.

The court also rejected Petitioners' contention that the favorable determination letter issued to the Plan in 1989 by the IRS protected the Plan from liability. The court concluded that the determination letter was "not owed any deference" because it did not specifically address the lump sum distribution methods used by the Plan. App. 33a. Consequently, "[t]he letter may protect the Plan from adverse tax treatment, but it does not protect the Plan from liability to its participants." *Id.* at 34a.

REASONS FOR GRANTING THE PETITION

This case concerns the freedom of an employer to design a cash balance retirement plan with account values that are perfectly apparent to the participants at any given time. The ruling below interferes with this ability by requiring sponsors to apply a convoluted valuation rule to determine the amount that must be distributed to separating employees who choose to withdraw a lump sum payment, rather than simply paying out the employee's account balance.[8] Nothing in ERISA required this; the IRS twice approved Petitioners' plan without the convoluted formula; and the IRS never expressed the view that the convoluted valuation formula should apply to cash balance plans until three years after Petitioners paid out Respondent's account balance.

The widespread use of cash balance plans warrants review by this Court to ensure that such plans are not saddled with unpredictable costs that produce windfalls for a few former employees to the detriment of others who may lose the benefits of such plans in the future.

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[8] In that respect, the court of appeals' decision contradicts the well established principle that employers and employees are free to determine whether and what kind of pension benefits an employer will provide. *See, e.g., Lockheed Corp.* v. *Spink*, 517 U.S. 882, 887 (1996) ("Nothing in ERISA requires employers to establish benefit plans. Nor does ERISA mandate what kind of benefits employers must provide if they choose to have such a plan.").

I. ERISA PERMITS "CASH BALANCE" PLANS TO PAY A DEPARTING EMPLOYEE WHO REQUESTS A "LUMP SUM" BENEFIT AN AMOUNT DETERMINED BY THE PLAN'S EXPRESS TERMS RATHER THAN BY A "PROJECTING FORWARD/DISCOUNTING BACK" FORMULA.

A. The Plain Language Of The Statute Applies Only To Non-Consensual Distributions.

The plain language of ERISA does not require that the value of a lump sum benefit be projected forward and then discounted back. The discount rate provided by the statute to calculate present value applies only "[f]or purposes of paragraph (1)," – *i.e.*, for purposes of determining whether a lump sum distribution can be made "without the consent of the participant." See ERISA § 203(e), 29 U.S.C. § 1053(e).

Despite this expressly limited "purpose" for § 203(e), the Eleventh Circuit concluded that the language was ambiguous. The court then went on, under a *Chevron* step-two analysis, to conclude that the Treasury Regulations were a reasonable interpretation of the statute. App. 24a-26a.

The court thus ignored the crystal clear limiting words of the statute in favor of reconstructing and expanding the stated legislative purpose.[9] The court should not have deviated from the "venerable principle that if the language of the statute is clear, that language must be given effect – at least in the absence of a patent absurdity." *INS* v. *Cardozo-Fonseca*, 480 U.S. 421, 452 (1987) (Scalia, J., concurring). The "for purposes of" language of the statute is perfectly clear, and remarkably specific, even if other provisions are less clear.

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[9] The court of appeals conceded that the statutory terms did not apply to consensual distributions but turned nonetheless to legislative history to broaden the text: "Although the text and the heading of the provision enacted in 1984 dealt only with calculating amounts for purpose of the restriction on mandatory distributions, the Senate Report spoke in broader terms." App. 12a n.10.

See generally Edward A. Zelinsky, *The Cash Balance Controversy*, 19 Va. Tax Rev. 683, 751 (2000). Paragraph (2) of ERISA § 203(e) plainly provided that, with respect to *whatever* calculations are specified in paragraph (2), they apply *only* "[f]or purposes of [determining whether a lump sum distribution can be made "without consent of the participant"]." 29 U.S.C. § 1053(e)(2).

The court erred by not focusing, as *Chevron* requires, on the plain language of the statute. 467 U.S. at 842-43. Where the fundamental dictate of the statute is clear and specific, it is up to Congress, not an administrative agency, to amend the statute. While *Chevron* recognizes that agencies may act to fill interstices within statutes, the mere presence of inconsistent language does not authorize rewriting the unambiguous provisions of the statute. See *K-Mart Corp.* v. *Cartier, Inc.*, 486 U.S. 281, 318 (1988) ("The authority to clarify an ambiguity in a statute is not the authority to alter even its unambiguous applications . . . .") (Scalia, J., concurring in part and dissenting in part). Thus, this Court should give effect to the specific and unambiguous limitation of § 203(e). See generally *Morales* v. *Trans World Airlines, Inc.*, 504 U.S. 374, 384 (1992) (applying the canon of statutory construction that "the specific governs the general").

Accordingly, the Treasury Department's decision to apply valuation requirements "whether or not the participant's consent is required," Treas. Reg. § 1.411(a)-11(d), conflicts with the plain language of § 203(e).

B. The Court Of Appeals Improperly Disregarded The Plan Administrator's Interpretation.

The court compounded its interpretation errors by blatantly disregarding the Plan administrator's own interpretation of the Plan on the precise question at issue here. The Plan administrator concluded that the Plan did not require additional interest credits to Respondent's account for periods after he withdrew his account balance from the Plan.

App. 84a. (In the Complaint, Respondent concedes that this interpretation of the Plan is correct. See Compl. ¶ 28.) Thus, the Eleventh Circuit's decision to import a projection forward requirement into the Plan (an issue not briefed before or decided by the district court) violates the principle established by this Court in *Firestone Tire & Rubber Co.* v. *Bruch*, 489 U.S. 101 (1989). *Firestone* instructs that an ERISA plan administrator's interpretation of the plan controls, absent abuse of discretion, if the plan delegates to the plan administrator the authority to interpret the plan. *Id.* at 111. The Plan contains precisely this kind of delegation, authorizing the administrator "to construe this Plan and resolve all equitable and other questions that arise under this Plan." Plan § 8.2 (App. 74a-75a).

C. A "Projection Forward" Requirement Cannot Be Inferred From The Law, The Regulations, Or The Plan.

Even if the Court were to look beyond the specific, limited "purposes" language of § 203(e), it is neither permissible nor reasonable for the court to interpret the statute or regulations to require cash balance plans to project interest credits forward to retirement age and then discount them back.

The court concluded that "Treasury Regulation § 1.411(a)-11(d) clearly provides that ERISA § 203(e), and the discount interest rates it prescribes, applies to consensual as well as non-consensual lump sum distributions" (App. 16a), but the court did not find that the law or regulations directly required the Plan to project interest credits forward. See *Id.* at 27a-32a. It is not until Notice 96-8, issued three years after the distribution to Respondent, that Treasury interpreted the statute or regulation to require cash balance plans to project interest credits forward. The court purports not to rely on Notice 96-8 (*id.* at 28a), but its analysis is unconvincing. The court merely says it was "skeptical about whether lack of guidance and direction can be a defense to this type of action by a plan participant, and in any event Treasury Regulation

§ 1.411(a)-11 when read against the Plan's own terms provides enough guidance that Georgia-Pacific is liable to plan participants even for distributions made before the issuance of IRS Notice 96-8." *Id.* at 29a-30a.

This is wrong on all counts. First, neither the statute nor the Regulation addresses anything other than discount rates, so they provide no basis whatever to infer a "projection forward" requirement. Without such a requirement there can be no discrepancy in interest rates, and thus no "whipsaw."

Second, even if § 203(e) were ambiguous, there is nothing in that section, or in Treasury Regulations §§ 1.411(a)-11 and 1.417(e)-1(d), that remotely requires a cash balance plan to project interest credits forward until retirement age.

Third, the Eleventh Circuit's passing observation that "the Plan itself" requires interest credits to be projected forward until age 65 (App. 32a) is completely untenable. The Plan unquestionably provides that employees may receive a "single lump sum payment" of the actual amount then credited to the employee's account. See Plan § 6.4(C) (*id.* at 74a) ("[A] participant . . . may elect to receive, in lieu of a standard form of benefit . . . a single lump sum payment equal to the amount credited to the Participant's Personal Account.")

Given this "lump sum" provision, the court's conclusion that Respondent "did not have a statutory right to the amount found in his hypothetical account prior to the normal retirement date" (*id.* at 31a) is inexplicable. The court looked right past the directly relevant provision of the Plan, and focused instead on the definitions of "normal retirement benefit," which is described in the Plan as an annuity starting at age 65, see Plan §§ 6.2, 6.3(a) (*id.* at 73a-74a) and "Accrued Benefit." Plan § 1.1 (*id.* at 73a). But neither of these provisions requires projecting forward. The court mistakenly relied on ERISA § 3(24), which merely states that the "accrued benefit" under a defined benefit plan is

"determined under the plan and . . . expressed in the form of an annual benefit commencing at normal retirement age. . . ." These definitions address the form of distribution at retirement age, but provide no hint of a "projecting-forward" requirement.[10] They provide no basis for the court's statement that "the Plan specifies that [Respondent's] hypothetical account balance must be projected forward using the interest credit rates set forth in the Plan." *Id.* at 32a. It does not. The court simply read too much into these provisions of the Plan, and read the "lump sum" provision completely out of the Plan.

In fact, it would have been ludicrous to design the Plan in a manner requiring it to pay interest credits after participants have chosen to withdraw their account. Indeed, under such a plan, the stated account balance would be meaningless and the retirement benefit would never be known to the employer or employees until after the whipsaw calculation. As the district court recognized, the "projecting forward" formula is no more than a "computational contrivance that has only slight connection with economic reality." App. 52a. In light of the Plan's directly applicable "lump sum" provision, this "computational contrivance" has no connection with the Plan either.

D. The "Projection Forward" Requirement Creates An Internal Conflict Within Treas. Reg. § 1.411(A)-11.

Treas. Reg. § 1.411(a)-11, which forms the principal basis for the Eleventh Circuit's decision, requires that participants give informed consent to retirement plan distributions exceeding the statutory threshold of $3,500 and goes on to

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[10] The Plan's definition of "Accrued Benefit" provides that a employee's plan account as of any given time can be expressed as a normal requirement annuity by dividing the account balance by the actuarial factors set forth in Appendix A of the Plan. *See* Plan § 1.1 (App. 73a).

state: "Furthermore, consent is not valid if a significant detriment is imposed under the plan on any participant who does not consent to a distribution." Treas. Reg. § 1.411(a)-11(c)(2)(i). Obviously, the Eleventh Circuit's holding that Respondent's "Accrued Benefit" under the Plan had to be whipsawed up to $49,314.83 if he took an immediate distribution, but was only $36,109.15 if he left it in the Plan, imposes a "significant detriment" on Respondent if he fails to consent to an immediate distribution. Indeed, he would lose the entire $13,000 difference (and more) if he declined to consent to an immediate distribution.[11] Thus, the Eleventh Circuit's holding conflicts with the regulation itself by forcing employees to take premature distributions from their retirement plans.

E. A "Projection Forward" Requirement Is Unreasonable For Cash Balance Plans.

The preceding discussion demonstrates that neither the law, the regulation, nor the Plan contains a "projection forward" requirement. Indeed, such a requirement is unreasonable in the context of a cash balance plan. Under a traditional defined benefit plan, it makes sense to calculate "present value" because the value of the benefit depends on how many years the employee will live to collect the fixed annuity. Calculating the *present* value of such a benefit requires an estimate of the employee's life span based on actuarial

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[11] The penalty for declining to consent to a distribution is even more severe when the age 65 (normal retirement) value of the benefit is considered. If Respondent had been paid $49,341.83 (as the Eleventh Circuit suggests), and had "rolled" the money into an individual retirement account and conservatively invested it earning the same return provided under the Plan, (PBGC "immediate" plus 75 basis points), he would have 27% more money 13 years later at age 65. For example, assuming an overall 6% rate of return under the Plan (which Respondent could easily match with conservative investments) he would have $105,242.58 at age 65 by taking an immediate distribution and only $77,018.22 if he refused to consent to an immediate distribution.

assumptions contained in a mortality table, and an interest rate to discount the value of the future payments back to when the lump sum benefit is paid.

By contrast, a cash balance plan requires *no* additional calculation to determine the present value of the employee's benefit at any given time. In cash balance plans, each employee's account balance reflects the "present value" of the employee's benefit (the total service credits and interest credits accumulated to date), so there is no need to use any "computational contrivance." App. 52a. Thus, there is no basis in law, regulation, or logic to require cash balance plans to project interest credits forward to age 65 and then discount them back to present value.

Applying the interpretation of ERISA § 203(e) and the regulations suggested by Respondent creates an irrational situation in which plan participants who elect to receive an early, lump sum benefit actually receive ***more than*** the "present value" of their retirement benefit. Stated differently, they receive the "present value" of their benefit (equal to the total pay and interest credits they have accumulated as of the distribution), *plus*, through the operation of whipsaw, a windfall that amounts to a payment of interest credits for years in which the plan participant neither works for the employer nor participates in the plan.[12] On the other hand, plan sponsors may suddenly face large and unexpected liabilities. Under Respondent's theory, Petitioners alone could be liable for millions of dollars in additional payments. See App. 7a, n.7. This is not consistent with ERISA's aspiration of uniformity and clarity in the administration of pension plans.

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[12] This permits participants effectively to earn a *double* interest, because the participant is able to withdraw the lump sum (including future interest credits) and then reinvest it elsewhere.

F. The IRS Specifically Approved Petitioners' Plan Including Its Interest Rate Limitations.

Faced with a statutory and regulatory scheme that did not address cash balance plans, Petitioners sought and obtained specific approval from the Treasury Department/IRS for the Plan's design. The IRS verified that the Plan complied with the applicable legal requirements. In cursory fashion, the Eleventh Circuit dismissed the 1989 favorable determination letter the Plan received from the IRS.[13] The court concluded the letter was "not owed any deference" (App. 33a) because such letters address only tax issues and "do not protect the Plan from liability to participants." *Id.* at 33a-34a. The Eleventh Circuit misconstrued the significance traditionally attached to IRS determination letters.

The IRS's own regulations establish the significance of the favorable determination letter provided to Petitioners. For example, Treas. Reg. § 601.201(a)(3), which was not addressed by the court below, provided as follows:

> A determination letter is issued only where a determination can be made on the basis of clearly established rules as set forth in the statute, Treasury decision, or regulation, or by a ruling, opinion, or court decision published in the Internal Revenue Bulletin.

Id.; see also ERISA § 3001(d), 29 U.S.C. § 1201(d) ("The Secretary of Labor shall accept the determination [letter issued to a plan applicant] of the Secretary of the Treasury as prima facie evidence of initial compliance by the plan with the standards of . . . this chapter [including ERISA § 203(e)]."). Moreover, the IRS checklists used to determine whether a plan is entitled to a favorable determination letter

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[13] The court rejected the 1997 determination letter in a footnote on the grounds that the determination was made after Respondent and those similarly situated with him had received their distributions. App. 34a n.30.

demonstrate the directly relevant, and conclusive, nature of the letter issued to the Plan. These checklists specifically require the agency to verify, *inter alia*, that the plan satisfies the IRC § 417 interest rate limitations, see Worksheet Number 2A – Determination of Qualification (Department of the Treasury – Internal Revenue Service) 2000, at V.g. (App. 77a), and that the plan's accrued benefit is "always ascertainable." *Id.* at VII.c.i. (App. 78a).

Thus, the fact that the IRS issued a favorable determination letter to the Plan confirms that the Plan's lump sum payment provisions either complied with, or were not governed by, the disputed regulations. The letter would not have been issued to Petitioners if the Plan failed to satisfy the IRC § 417/ERISA § 203(e) interest rate limitations invoked by the Respondent.

G. The Plan Also Qualified For The IRS "Safe Harbor."

The Plan also satisfied the terms of the safe harbor provision established by Notice 96-8. Under Notice 96-8, "for plan years beginning before the regulations are effective,"[14] a plan will "not be disqualified for failing to satisfy section 411(a) or 417(e) if the amount of the distribution satisfied those sections based on a reasonable, good faith interpretation of the applicable provisions of the Code, taking into account pre-existing guidance." App. 71a. For the reasons stated previously, and for the very lack of "pre-existing guidance," the Plan's decision to pay Respondent an amount equal to his account balance can be viewed as nothing less than a "reasonable, good faith interpretation" of existing law. Even so, the Eleventh Circuit summarily dismissed this safe harbor. See *id.* at 30a n.28.

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[14] As of January 2001, these regulations still have not been promulgated.

H. Forcing Plans To Reduce Interest Crediting Rates To Avoid Whipsaw Harms Participants.

The court of appeals suggested a bizarre solution to the legal and political havoc it wrought. To prevent former employees like Respondent from receiving pre-retirement windfalls, the court suggested plan sponsors need only "reduce any perceived disparity by reducing or eliminating the difference between the statutory discount rate . . . and the interest credit rate." App. 24a. In other words, employers should cut the rate of return to the detriment of all employees (and former employees who leave their account balances in the plan).

Given the widespread use and benefits of cash balance plans, the numerous defects in the court of appeals' analysis make review by this Court appropriate.

II. THE COURT OF APPEALS' SUMMARY DISMISSAL OF THE FAVORABLE IRS DETERMINATION LETTER ISSUED TO THE PLAN SUBJECTS EMPLOYERS TO INCONSISTENT LIABILITIES UNDER ERISA AND THE TAX CODE.

The Eleventh Circuit's decision also violates the statutory plan for ERISA by subjecting employers to inconsistent liabilities under ERISA and the parallel provision of the Internal Revenue Code, contrary to ERISA § 3002(c) (29 U.S.C. § 1202(c)) and Reorganization Plan No. 4 of 1978, 92 Stat. 3790. By relegating the favorable IRS determination letters issued to the Plan and Notice 96-8's "safe harbor" provisions (for which the Plan qualifies) only to tax qualification matters (App. 30a n.28, 34a & n.30.), the decision below opens up a chasm between tax and pension law that Congress did not intend.

Under the Eleventh Circuit's decision, a cash balance plan can be certified as "tax qualified" in IRS determination letters and be in complete compliance with the safe harbor

provisions of Notice 96-8, but still be held liable to plan participants for violating the identical provisions of Title I, Subtitle B, of ERISA, such as § 203(e). For example, Notice 96-8 allows cash balance plan sponsors to comply with ERISA § 203(e) and Treas. Reg. §§ 1.411(a)-11 and 1.417(e)-1(d) by using a "safe harbor" interest crediting rate equal to the prevailing three-month Treasury bill rate plus 175 basis points (1.75%). App. 70a. This "safe harbor" rate has exceeded the Code § 417(e) discount rate (30-year T-bills) in all but two months since July 1, 1996. See Federal Reserve Statistical Release H.15. This "spread" has exceeded 100 basis points (1.0%) in several months, which is greater than the "spread" in the Plan's interest crediting rate cited by the Eleventh Circuit as the basis for Respondent's whipsaw claim (0.75%). Thus, even plans that comply with the letter of Notice 96-8 *after* its issuance may be subject to "whipsaw" lawsuits under Title I of ERISA under the court of appeals' decision.

This dichotomy conflicts starkly with the congressional desire to ensure consistency in the administration of ERISA. ERISA establishes substantively identical requirements under Title I, Subtitle B, Part 2, 29 U.S.C. § 1132(a), which is administered by the Department of Labor, and Title II, Subtitle A, Part 1, 29 U.S.C. § 1053(e), which is administered by the IRS. In order to ensure that the rules were consistent, Congress provided in ERISA § 3002(c) and Reorganization Plan No. 4 that regulations provided by the Treasury Department/IRS would also apply to the standards established under Title I and administered by the Department of Labor. See ERISA § 3002(c), 29 U.S.C. § 1202(c) ("Regulations prescribed by the Secretary of Treasury under [the] . . . minimum vesting standards . . . shall also apply to the . . . [minimum vesting] standards set forth in parts 2 and 3 of subtitle B of subchapter I of this chapter."); Reorganization Plan No. 4 of 1978, § 104, 92 Stat. at 3791 (in pursuing civil actions to enforce "Parts 2 and 3 of Subtitle B of Title I of

ERISA . . . the Secretary of Labor shall be bound by the regulations, rulings, opinions, variances, and waivers issued by the Secretary of Treasury").[15] Review of the court of appeals decision is necessary to restore the congruence between ERISA and the Tax Code as specified by Congress.

III. PETITIONERS DID NOT RECEIVE FAIR NOTICE OF A PURPORTED IRS REQUIREMENT THAT "CASH BALANCE" PLANS APPLY A "PROJECTING FORWARD/DISCOUNTING BACK" FORMULA.

The Eleventh Circuit's decision to construe Treasury regulations as imposing a project forward/discount back requirement on the Plan violates the "fair notice" doctrine. Petitioners had no reason to believe, when they provided a lump sum distribution to Respondent, that they were required to pay Respondent an additional $13,000 in interest credits for years *after* his withdrawal from the Plan.

The Eleventh Circuit rejected Petitioners' contention that they did not have sufficient notice of the purported regulatory scheme. See App. 29a-30a. In so doing, the court failed to address adequately a fundamental principle of due process: in enforcing an agency's interpretation of law, "[t]raditional concepts of due process incorporated into administrative law preclude an agency from penalizing a private party for

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[15] The court of appeals itself cited the rationale for this parallelism: "'The reason that many ERISA sections have such counterparts is that, to encourage employers to establish pension plans, Congress provides favorable tax treatment for plans which comply with ERISA.'" App. 14a n.13 (quoting *Gillis* v. *Hoechst Celanese Corp.* 4 F.3d 1137, 1144 n.6 (3d Cir. 1993)); *see also Rybarszyk* v. *TRW, Inc.*, No. 97-4167, 2000 WL 1862664, at *10 (6th Cir. Dec. 21, 2000) ("ERISA provides that regulations promulgated by the Treasury Department pursuant to I.R.C. §§ 410(a), 411, and 412 are deemed applicable to the parallel provisions of ERISA. 29 U.S.C. § 1202(c)."); *McDaniel* v. *Chevron Corp.*, 203 F.3d 1099, 1115 (9th Cir. 2000) ("[R]ules prescribed under § 411 of the I.R.C. apply with equal force to § 204 of ERISA.").

violating a rule without first providing adequate notice of the substance of the rule." *Satellite Broad. Co.* v. *FCC*, 824 F.2d 1, 3 (D.C. Cir. 1987).[16]

The standards for evaluating whether a party has fair notice of an agency interpretation have been developed primarily in a line of D.C. Circuit cases. In an action where, as here, there is no specific, pre-enforcement warning, the following standard applies:

> [W]e must ask whether the regulated party received, or should have received, notice of the agency's interpretation in the most obvious way of all: by reading the regulations. If, by reviewing the regulations and other public statements issued by the agency, a regulated party acting in good faith would be able to identify, with "ascertainable certainty," the standards with which the agency expects the party to conform, then the agency has fairly notified a petitioner of the agency's interpretation.

General Elec. Co. v. *EPA*, 53 F.3d 1324, 1329 (D.C. Cir. 1995); see also *Trinity Broad., Inc.* v. *FCC*, 211 F.3d 618, 628 (D.C. Cir. 2000); *PDM Produce Brokerage Corp.* v. *USDA*, Civ. No. 00-1163 (D.C. Cir. Dec. 19, 2000) (applying the same standards).

In this case, a regulated party acting in good faith prior to Notice 96-8 would not have been able to identify with "ascertainable certainty" that the regulations relied upon by

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[16] Regardless of who is imposing the penalty (an agency or, as here, a court at the invitation of a private party), principles of fair notice require adequate notice of an agency's interpretation of a particular rule. *See generally, United States* v. *Chrysler Corp.*, 158 F.3d 1350, 1357 (D.C. Cir. 1998) (reversing an automobile recall ordered by the district court where the automobile manufacturer did not receive fair notice of the interpretation of an NHTSA safety standard); *Diamond Roofing Co.* v. *OSHRC*, 528 F.2d 645, 649 (5th Cir. 1976) ("An employer . . . is entitled to fair notice in dealing with his government.").

Respondent required the Plan to project interest rates forward and then discount them back. As explained in Part I, *supra*, neither the language of the regulations nor the statutory provision (§ 403(e)) is clear on this issue. Moreover, any such calculation would not logically apply in any event, because the "present value" of the benefit is already expressed as the employee's account balance. Cf. *United States* v. *Chrysler Corp.*, 158 F.3d 1350, 1357 (D.C. Cir. 1998) ("Chrysler might have satisfied NHTSA with the exercise of extraordinary intuition or with the aid of a psychic, but these possibilities are more than the law requires.").

There cannot be any real dispute that the plan administrator acted in good faith when he informed Respondent that the regulations did not apply because cash balance plans were a "special form" of plan. App. 83a. To the extent that there were any other "public statements" prior to 1996, they support Petitioners' interpretation of the regulations. First, in 1989, the Plan received a determination letter that it was tax qualified, a certification that cannot be made without the IRS verifying that the lump sum benefit calculations used by the Plan complied with the regulations. *Id.* at 86a.

Second, Notice 96-8 provides compelling evidence that the agency itself recognized that the regulatory structure, as it applied to cash balance plans, was anything but clear. The Notice recognized a lack of prior guidance and provided a safe harbor provision, an unnecessary measure if the regulations alone provided adequate notice. Furthermore, the Notice expressly stated that it provided only "proposed guidance . . . in anticipation of regulations that incorporate the proposed guidance." App. 60a. Tellingly, these regulations still have not been promulgated.

The agency's implicit concession that the regulations were unclear is particularly important in determining whether the regulated entity received fair notice. Thus, in *Trinity Broadcasting*, the D.C. Circuit placed considerable weight on

the fact that the FCC in previous proceedings had determined that similar rules were sufficiently unclear as to be unenforceable. See 211 F.3d at 631; see also *General Elec.*, 53 F.3d at 1333-34 ("Where, as here, the regulations and other policy statements are unclear, where the petitioner's interpretation is reasonable, and where the agency itself struggles to provide a definitive reading of the regulatory requirements, a regulated party is not 'on notice' of the agency's ultimate interpretation of the regulations, and may not be punished."). The same reasoning applies here: it would be manifestly unjust for the agency to conclude, on the one hand, that the regulations were unclear prior to 1996 and then request, on the other, that the regulations be enforced against Petitioners for all distributions occurring prior to 1996. See generally *Chrysler Corp.*, 158 F.3d at 1356 ("an agency is hard pressed to show fair notice when the agency itself has taken action in the past that conflicts with its current interpretation"). This conflict provides an independent and reinforcing justification for the Court's review of the decision of the court of appeals in this case.

CONCLUSION

For the foregoing reasons, the petition for writ of certiorari should be granted.

Respectfully submitted,

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January 23, 2001

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APPENDIX A

UNITED STATES COURT OF APPEALS
ELEVENTH CIRCUIT

No. 99-10640

JERRY L. LYONS, individually and on behalf of all other persons similarly situated,

Plaintiff-Appellant,

v.

GEORGIA-PACIFIC CORPORATION SALARIED EMPLOYEES RETIREMENT PLAN, GEORGIA-PACIFIC CORPORATION,

Defendants-Appellees.

Aug. 11, 2000

Appeal from the United States District Court for the Northern District of Georgia.

Before CARNES, BARKETT and WILSON, Circuit Judges.

CARNES, Circuit Judge:

This is an Employee Retirement Income Security Act ("ERISA"), 29 U.S.C. § 1001, *et. seq.*, case in which we are called upon to decide issues about how to calculate a consensual, lump sum payout in a front-loaded, defined benefit, cash balance pension plan with fixed interest credits. The principal issue is whether such a payout must be calculated using the present value methodology set out in

Treasury Regulations 1.411(a)-11 and 1.417(e)-1,[1] the former of which the district court held to be invalid. *See Lyons v. Georgia-Pacific Corp. Salaried Employees Retirement Plan*, 66 F.Supp.2d 1328, 1336 (N.D.Ga.1999). For reasons we will explain, we are convinced that those Treasury regulations are valid and control the calculation of consensual lump sum payouts, at least insofar as they apply to distributions that occurred prior to the effective date of the amendments that the Retirement Protection Act of 1994 made to ERISA § 203(e), 29 U.S.C. § 1053(e).

I. BACKGROUND

A. The Plan

There are two basic types of pension plans, defined contribution plans and defined benefit plans. A defined contribution plan provides for each participant a separate account to which contributions are made, with the retirement benefit depending on the amounts that have been contributed to the account and the investment gains and losses on the amounts in the account. *See* ERISA § 3(34), 29 U.S.C. § 1002(34); *see also* Barbara J. Coleman, *Primer on Employee Retirement Income Security Act* 32-33 (4th ed.1993). No specific, defined retirement amount is promised under a defined contribution plan. *See id.* The plan involved in this case is not of that type.

Instead, this case involves a defined benefit plan, which is one where the retirement benefit is expressed as a certain annual amount to be paid by the employer over the employee's lifetime, beginning at the employee's retirement. *See* ERISA § 3(35), 29 U.S.C. § 1002(35). Such a plan promises a specific defined benefit the calculation of which is

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[1] Treasury Regulations 1.411(a)-1 and 1.417(e) were promulgated in 1988 and were later amended in 1994. All of our references to these regulations refer to the 1988 versions.

not dependent upon investment gains or losses. *See* Coleman, *supra*, at 32-33. There are subtypes of defined benefit plans. The one involved in this case is a cash balance defined benefit plan.

At all times relevant to this case, the Georgia-Pacific Corporation Salaried Employees Retirement Plan ("the Plan") has been a cash balance plan, which is a defined benefit plan that determines benefits for each employee by reference to the amount of the employee's hypothetical account balance. An employee's hypothetical account balance is credited by the employer with hypothetical allocations and hypothetical interest earnings determined under a formula set forth in the Plan. The hypothetical allocations and hypothetical earnings are designed to resemble actual contributions and earnings under a defined contribution plan. *See* I.R.S. Notice 96-8, 1996-1 C.B. 359, 1996 WL 17901. One benefit of cash balance plans is that they "allow younger workers to take a larger benefit with them when changing jobs." *Give Employees Meaningful Information When Pensions are Changed to Cash Balance Plans, Says Actuary*, PR Newswire, May 7, 1999.[2]

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[2] The first cash balance plan was introduced in 1985 for BankAmerica Corporation. *See* Lindsay Wyatt, *"Hybrid" Plans Fit Evolving Workforce*, Pension Management, March, 1996; *see also* Richard D. Brown, *An Introduction to Basic Employee Retirement Benefits*, 340 P.L.I. 7, 82 (1993) ("The Cash Balance Plan is a modified form of defined benefit pension plan which was introduced by the actuarial firm of Kwasha Lipton in the mid-1980's."). Since then, many large companies such as BellSouth Corp., Xerox Corp., Countrymark Cooperative, and Blue Cross/Blue Shield of New Jersey have adopted these plans. *See* Wyatt, *supra*. More than 300 companies, with hundreds of billions of dollars in pension assets, have switched from traditional pension plan formulas to cash balance plans. *See Q*-and-*A*: *What You Need to Know About Today's "Cash-Balance" Plans*, Payroll Manager's Report, Feb. 2000, at 3.

Section 3.1 of the Plan requires that a hypothetical bookkeeping account—the Personal Account—be established and maintained for each participant. Each month the participant's Personal Account is credited with (1) *service credits*, a specified percentage of the participant's compensation for that month; and (2) *interest credits*, which are derived by multiplying the hypothetical balance in the Personal Account by the Periodic Adjustment Percentage. That adjustment percentage is computed under the Plan by determining the Pension Benefit Guaranty Corporation ("PBGC")[3] twelve-month "immediate" annuity interest rate for the preceding year, then adding .75% to that rate, and, lastly, dividing this composite annual rate by 12. Under ERISA the Plan could have used an adjustment percentage equal to the prescribed maximum PBGC rate, but instead it used a higher rate. If the Plan had not used a higher adjustment rate, the dispute in this case would never have arisen, but more about that later.

Although service credits cease when the participant leaves employment, interest credits continue until the participant's Benefit Commencement Date. That is why the Plan is said to be a "front-loaded" interest credit plan, defined as one in which "future interest credits to an employee's hypothetical account balance are not conditioned upon future service." I.R.S. Notice 96-8 at 4. In the case of an annuity form of benefit under this Plan, the Benefit Commencement Date is the date that the annuity is payable. Thus, if the participant is entitled to an annuity that is payable at age 65, under the

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[3] The Pension Benefit Guaranty Corporation is "a wholly owned United States Government corporation . . . modeled after the Federal Deposit Insurance Corporation," whose Board of Directors "consists of the Secretaries of the Treasury, Labor, and Commerce." *Pension Benefit Guaranty Corp. v. LTV Corp.*, 496 U.S. 633, 636-37, 110 S.Ct. 2668, 2671, 110 L.Ed.2d 579 (1990). It "administers and enforces Title IV of ERISA." *Id.* at 637, 110 S.Ct. at 2671.

front-loaded aspect of the Plan, interest credits continue to accrue until age 65, even if the participant separates from employment with Georgia-Pacific before age 65.

Under the Plan a participant may elect, under certain specified conditions, to receive his accrued pension benefits in an optional lump sum form, payable immediately, rather than as an annuity commencing at age 65. If the participant elects this option, the amount payable under the Plan is a single sum equal to the amount in the participant's Personal Account (the hypothetical bookkeeping account).[4] It is this feature of the plan—the provision that the lump sum payout is the amount in the Personal Account at the time—that is at issue in this case.

B. Facts

From 1965 until 1990, Jerry L. Lyons was employed as a paper inspector and paper tester for Great Northern Corporation. In 1990, Georgia-Pacific Corporation acquired Great Northern. As a result of the acquisition, Lyons became an employee of Georgia-Pacific, Great Northern's pension plan was merged with the Georgia-Pacific Salaried Employees Retirement Plan (which we are calling "the Plan"), and Lyons became a participant of it.

On January 5, 1991, Lyons left employment at Georgia-Pacific. In accordance with Article 4 of the Plan, Lyons was entitled to a vested benefit, because he had worked for Georgia-Pacific and Great Northern for at least five years. Pursuant to section 1.1 of the Plan, Lyons' accrued pension benefit was an annuity commencing at age 65. In November 1992, Lyons elected to receive his accrued pension benefit in

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[4] Under the Plan at Section 6.4(a), "Option C" is:

> A single lump sum payment equal to the amount credited to the Participant's Personal Account as of the end of the month preceding his Benefit Commencement Date.

the optional lump sum form, payable immediately, as he was permitted to do under section 6.4(a) of the Plan. Consistent with the Plan's payout provision for lump sums, Georgia-Pacific distributed to Lyons in January of 1993 a lump sum equal to the amount credited to his Personal Account—$36,109.15. *See Lyons*, 66 F.Supp.2d at 1329, 1332.

Two months after receiving his lump sum, Lyons consulted with the National Center for Retirement Benefits ("NCRB")[5] and was told by it that Georgia-Pacific had distributed to him substantially less than the amount he was entitled to receive under ERISA § 203(e), *see* 29 U.S.C. § 1053(e), at least as that statutory provision had been interpreted in Treasury Regulation 1.411(a)-11 and Treasury Regulation 1.417(e)-1.

We will discuss those Treasury regulations more later, but at this juncture it is enough to say that Georgia-Pacific did not follow them. If it had, instead of merely paying Lyons a lump sum equal to the amount credited to his Personal Account, which was $36,109.15, Georgia-Pacific would have taken the value of the annuity Lyons would have received at age 65 and discounted it to present value by using the PBGC rate.[6] That approach, following the Treasury regulations, would have yielded Lyons a lump sum payout of $49,341.83. *See Lyons*, 66 F.Supp.2d at 1332. The validity of the

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[5] The NCRB is a for-profit consulting firm that works on a contingent fee basis reviewing pension payouts on behalf of individual participants and advocating for them at the administrative level. *See Senate Committee Holds Hearing on Pension Benefit Miscalculations*, Pension & Benefits Week Newsletter (RIA Group), June 23, 1997. Where its administrative representation proves unsuccessful, the NCRB has been known to refer cases to attorneys for class action lawsuits. *See Mathews v. Sears Pension Plan*, No. 95 C 1988, 1996 WL 199746, at *5 (N.D.Ill. April 23, 1996).

[6] At that time the PBGC rate was approximately 4.5 percent. *See Lyons*, 66 F.Supp.2d at 1336.

Treasury regulations is thus a question worth $13,232.68 to Lyons.[7]

C. Procedural History

In a letter dated March 18, 1996, the NCRB, acting on behalf of Lyons, advised Georgia-Pacific that Treasury Regulation 1.417(e)-1 requires a minimum lump sum payable from a defined benefit plan to be no less than the present value of the participant's normal retirement benefit; and that the present value of Lyons' normal retirement benefit exceeded the amount in his Personal Account, which was the amount he was paid. The NCRB's letter requested that Georgia-Pacific recalculate Lyons' benefit in accordance with Treasury Regulation 1.417(e), and pay Lyons the shortfall.

Georgia-Pacific responded to the NCRB on April 17, 1996, taking the position that: the Plan is a "special" form of defined benefit plan known as a "cash balance plan;" IRS Notice 96-8 notes that cash balance plans define benefits for each employee by reference to a hypothetical account balance; most cash balance plans permit the distribution of an employee's accrued benefit in the form of a single sum equal to the employee's hypothetical account balance; Lyons' "lump sum distribution was not calculated with reference to the present value of a normal retirement benefit;" and instead, the amount distributed to Lyons was the amount credited to his Personal Account.

On April 14, 1997, Lyons, on behalf of himself and other similarly situated persons, filed a class action complaint against Georgia-Pacific and the Plan (collectively "Georgia-Pacific") alleging that the method used to pay lump sum cash distributions under the Plan violated ERISA § 203(e)(2), 29

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[7] At oral argument counsel for Lyons and the class stated that the difference for the class as a whole could be around $20 million.

U.S.C. § 1053(e)(2).[8] After Georgia-Pacific answered the complaint, the district court in September of 1997 certified a class under Rule 23(b)(3), and it defined the class as follows:

> All participants (or beneficiaries of participants) in the [Plan] (i) who received a lump sum distribution of benefits calculated at a time when such participants had a vested interest in the Plan and who (ii) received a distribution of benefits in a lump sum where (iii) at the date as of which the amount of the lump sum was calculated, the lump sum was lower than the present value, if determined using the "applicable interest rate" as defined in Internal Revenue Code Section 417(e)(3) and set forth in Treasury Regulations issued pursuant to Internal Revenue Code Section 417(e), of such participants' accrued benefit, as defined under ERISA.

Dist. Ct. Consent Order (September 29, 1997). Thereafter, the parties informed the district court that they "would prefer to seek a ruling from the Court as to the threshold issue of potential liability as to any class member before engaging in costly and time consuming discovery on issues pertaining to individual class members (or groups thereof), damages, or class membership." Dist. Ct. Consent Order (March 11, 1998). On March 11, 1998, the court accommodated the parties by entering a consent order permitting them to file summary judgment motions on that threshold liability issue. *See id.* at 1-2. The order provided that if the court's ruling on that issue did not dismiss or otherwise resolve the case, there would be a period during which the parties could "conduct discovery on issues pertaining to defenses as to claims of

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[8] Lyons has standing to sue for benefits because he was a participant in the Plan as defined by ERISA § 3(7). *See* 29 U.S.C. § 1002(7); *see generally Firestone Tire & Rubber Co. v. Bruch*, 489 U.S. 101, 115-18, 109 S.Ct. 948, 957-58, 103 L.Ed.2d 80 (1989) (interpreting the term "participant" in § 1002(7)).

individual class members or groups thereof, class membership, damages, and similar issues." *Id.* at 2.

In its ensuing motion for summary judgment, Georgia-Pacific argued that the interest rate restrictions set forth in ERISA § 203(e)(2) apply exclusively to involuntary lump sum distributions of $3,500 or less, and because Lyons and the other class members received a voluntary lump sum distribution, the statute was inapplicable. Georgia-Pacific further argued that: ERISA § 204(c)(3) and Internal Revenue Code ("IRC") § 411(c)(2) permitted distribution of the Personal Account as the entire accrued benefit; Georgia-Pacific was entitled to rely upon a good faith exception in IRS Notice 96-8 (a notice Lyons argued supports his claim); and two IRS determination letters exonerated it from liability.

On March 22, 1999, the district court granted summary judgment for Georgia-Pacific. Relying upon the statutory language cited by Georgia-Pacific, the court held that the interest rate provisions contained in ERISA § 203(e)(2) apply only for the purpose of determining if a participant must consent to the distribution of a lump sum, and there exists no legislative authority in either the language of the statute or elsewhere requiring lump sum distributions to be computed in accordance with those interest rate provisions. Therefore, the court concluded, Treasury Regulation 1.411(a)-11 was "an unreasonable construction of . . . ERISA § 203(e)." *Lyons*, 66 F.Supp.2d at 1336.

On April 2, 1999, the district court entered an amended order and final judgment, certifying the class under Federal Rule of Civil Procedure 23(b)(1)(A) and Federal Rule of Civil Procedure 23(b)(2). The court made no change in the definition of the class. Lyons timely appealed the amended order and final judgment.

II. DISCUSSION

The principal dispute in this case is about whether ERISA § 203(e), 29 U.S.C. § 1053(e), and the Treasury regulations interpreting that provision required Georgia-Pacific to calculate Lyons' lump sum benefit by determining the amount he would have received at the normal retirement age of 65 and then discounting that amount back to the present value using the PBGC discount rate. It may help to explain why that matters.

As we have said, because the Plan is "front-loaded," interest credits to a participant's Personal Account continue after separation from employment until the normal retirement date, which is specified by the Plan to be age 65. Another important feature of the Plan is that the interest credit rate it provides is higher than the maximum discount rate prescribed in ERISA § 203(e). As a result, if the Plan's interest credit rate is applied to the Personal Account balance at separation and projected forward to determine what the normal retirement benefit would be at age 65, and that benefit is then reduced to a present value using the maximum discount rate, the resulting amount will be more than what is in the Personal Account before the calculations are done.[9] The amount of the difference will be the result of two factors—the time until age 65 (the longer the time, the greater the difference) and the amount the interest credit rate exceeds the prescribed maximum discount rate (the more it does, the greater the difference). Pinning our explanation to the facts of this case, the difference of $13,232.68 between the balance in Lyons' Personal Account, which is what he was paid under the Plan, and the amount he claims he is entitled to results from the .75

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[9] Stated another way, but equally true, when a cash balance plan's interest credit rate is greater than the discount rate applied, the participant's account balance will be less than the present value of the normal retirement benefit.

percent difference between the higher interest credit rate established in the Plan and the discount rate prescribed by PBGC, carried over the time between the payout of his lump sum distribution and his normal retirement date. If the plan had pegged the interest credit rate to the prescribed maximum discount rate, there would have been no difference (regardless of the time factor), and no dispute. But it did not, so there is a dispute.

The district court held that the Treasury regulation requiring that any lump sum cash payout be calculated by applying the PBGC discount rate to the normal retirement benefit under the plan was invalid. We review that holding *de novo*. *See Lee v. Flightsafety Services Corp.*, 20 F.3d 428, 431 (11th Cir.1994).

A. The Statute, Code Sections, and Regulations

In 1974, Congress enacted ERISA, 29 U.S.C. § 1001, *et. seq.*, to protect the interests of employees by ensuring that they received the pension benefits to which they were entitled. *See* ERISA § 2, 29 U.S.C. § 1001. Ten years later, Congress enacted the Retirement Equity Act, which amended ERISA and the Internal Revenue Code to "improve the delivery of retirement benefits and provide for greater equity under private pension plans for workers and their spouses and dependents. . . ." S.Rep. No. 98-575 (1984), *reprinted in* 1984 U.S.C.C.A.N. 2547. As part of that 1984 legislation, Congress added § 203(e) to ERISA and a materially identical § 417(e) to the Internal Revenue Code. Those added provisions made the PBGC rate the maximum interest rate a plan could use to discount to present value a normal retirement benefit for purposes of determining whether the amount to be distributed exceeded the cap on involuntary lump sum distributions. After the 1984 enactment, ERISA § 203(e) read in its entirety as follows:

(e) Restrictions on mandatory distributions

(1) If the present value of any accrued benefit exceeds $3,500, such benefit shall not be treated as nonforfeitable if the plan provides that the present value of such benefit could be immediately distributed without the consent of the participant.

(2) For purposes of paragraph (1), the present value shall be calculated by using an interest rate not greater than the interest rate which would be used (as of the date of the distribution) by the Pension Benefit Guaranty Corporation for purposes of determining the present value of a lump sum distribution on plan termination.

ERISA § 203(e), 29 U.S.C. § 1053(e) (1985).[10]

Two years later, Congress enacted the Tax Reform Act of 1986. Among other things, that legislation amended ERISA § 203(e)(2) and the parallel IRC § 417(e)(3) by adding new

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[10] Although the text and the heading of the provision enacted in 1984 dealt only with calculating amounts for purposes of the restriction on mandatory distributions, the Senate Report spoke in broader terms. The pertinent part of it said:

> *For purposes of determining the present value of the participant's benefit*, the bill provides that a plan may not use an interest rate that is greater than the rate used by the Pension Benefit Guaranty Corporation (PBGC) for valuing a lump sum distribution upon plan termination.
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> *For purposes of calculating the present value of a benefit as of the date of the distribution*, the plan is required to use an interest rate no greater than the rate used by the Pension Benefit Guaranty Corporation (PBGC) in valuing a lump sum distribution upon plan termination . . .

S. Rep. No. 98-575 (1984), *reprinted in* 1984 U.S.C.C.A.N. at 2549, 2562 (emphasis added). This legislation was not specifically tailored to cash balance plans—which did not even begin to appear until 1985, *see supra* n.2—but was instead aimed at defined benefit plans in general.

provisions relating to the calculation of the present value of an accrued benefit. One of those provisions permitted the use of a discount rate up to 120% of the applicable PBGC interest rate if the vested accrued benefit exceeded $25,000 using the PBGC rate. The other provision clarified that the present value determined under the 120% rate could not be less than $25,000. *See* Tax Reform Act of 1986, Pub.L. No. 99-514, §§ 1139(b), (c), 100 Stat. 2085.

After those amendments were made in the Tax Reform Act of 1986, this is how ERISA § 203(e) read:

> (1) If the present value of any nonforfeitable benefit with respect to a participant in a plan exceeds $3,500, the plan shall provide that such benefit may not be immediately distributed without the consent of the participant.
>
> (2)(A) For purposes of paragraph (1), the present value shall be calculated—
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> (i) by using an interest rate no greater than the applicable interest rate if the vested accrued benefit (using such rate) is not in excess of $25,000,
> and
>
> (ii) by using an interest rate no greater than 120 percent of the applicable interest rate if the vested accrued benefit exceeds $25,000 (as determined under clause (i)).
>
> In no event shall the present value determined under subclause (II)[sic] be less than $25,000.
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> (B) For purposes of subparagraph (A), the term "applicable interest rate" means the interest rate which would be used (as of the date of the distribution) by the Pension Benefit Guaranty Corporation for purposes of determining the present value of a lump sum distribution on plan termination.

> (3) This subsection shall not apply to any distribution of dividends to which section 404(k) of Title 26 applies.

29 U.S.C. § 1053(e) (1990).[11] This subsection of ERISA, and the parallel Internal Revenue Code subsection, have been amended several times since the Tax Reform Act of 1986. However, none of those amendments occurred until after Lyons had elected in November of 1992 to receive his lump sum benefit and had been paid it in January of 1993. We will confine our analysis to the law applicable to Lyons and those similarly situated.[12]

Many ERISA sections have parallel provisions in the Internal Revenue Code, tax provisions that are worded in ways materially identical to the ERISA sections.[13] ERISA

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[11] In 1989, Congress enacted the Omnibus Budget Reconciliation Act of 1989. That Act made minor changes to paragraph (1) of ERISA § 203(e), but did not alter paragraph (2), which is the relevant paragraph in this case. *See* Omnibus Budget Reconciliation Act of 1989, P.L. 101-239, §§ 7682, 7891, 103 Stat. 2106, 2434, 2445.

[12] One amendment in particular, made by the Retirement Protection Act of 1994, may have altered the legal landscape insofar as Treasury Regulation 1.411(a)-11 is concerned. *See* Retirement Protection Act of 1994, P.L. 103-465, § 767(c), 108 Stat. 4809, 5039 (codified as amended at 29 U.S.C. § 1053(e)); *see also infra* 26-27. That amendment may or may not portend a different result for plan participants who received lump sum distributions after its effective date. But Lyons received his distribution before the effective date of the 1994 legislation, and is therefore not affected by it. *See infra* n. 31. When we refer throughout this opinion to those "similarly situated" to Lyons, we mean in terms of that amendment, i.e., those who received their distributions before the effective date of the Retirement Protection Act of 1994 amendment to ERISA § 203(e).

As we will discuss later, there are class representation problems relating to those who elected lump sum payouts and received them after the effective date of the Retirement Protection Act of 1994. *See infra* Part II. E.

[13] "The reason that many ERISA sections have such counterparts in the IRC is that, to encourage employers to establish pension plans, Congress

§ 203(e) is such a provision. Its tax counterparts are IRC §§ 411(a)(11) and 417(e). ERISA itself provides that Treasury regulations promulgated under IRC §§ 410(a), 411 and 412 are equally applicable to the parallel provisions of ERISA. *See* ERISA § 3002(c), 29 U.S.C. § 1202(c)[14]; 29 C.F.R. § 2530.200a-2 ("Regulations prescribed by the Secretary of the Treasury or his delegate under sections 410 and 411 of the [Internal Revenue] Code (relating to minimum standards for participation and vesting) shall apply for purposes of sections 202 through 204 [of ERISA]"); *Williams v. Cordis Corp.*, 30 F.3d 1429, 1431 n. 2 (11th Cir.1994); *see also* 26 U.S.C. § 7805 ("[T]he Secretary [of the Treasury] shall prescribe all needful rules and regulations for the enforcement" of the Internal Revenue Code.).

Because of the law discussed in the preceding paragraph, Treasury Regulation 1.411(a)-11 which interprets IRC § 411(a)(11) is equally applicable to ERISA § 203(e). That Treasury regulation, which was issued in 1988, sets forth the same discount rate restrictions as ERISA § 203(e), but goes further to clearly specify that the present value of *any* optional form of benefit (a lump sum payout is an optional form of benefit), cannot be less than the present value of the participant's normal retirement benefit. Treasury Regulation 1.411(a)-11 states in pertinent part:

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provides favorable tax treatment for plans which comply with ERISA's requirements." *Gillis v. Hoechst Celanese Corp.*, 4 F.3d 1137, 1144 n. 6 (3rd Cir.1993) (citation omitted).

[14] ERISA § 3002(c) provides:

> Regulations prescribed by the Secretary of the Treasury under [Internal Revenue Code] sections 410(a), 411 and 412 of Title 26 (relating to minimum participation standards, minimum vesting standards, and minimum funding standards, respectively) shall also apply to the minimum participation, vesting and funding standards set forth in parts 2 and 3 of subtitle B of subchapter I of this chapter.

> (a) Scope—(a)(1) In general. Section 411(a)(11) restricts the ability of a plan to distribute any portion of a participant's accrued benefit without the participant's consent. *Section 411(a)(11) also restricts the ability of defined benefit plans to distribute any portion of a participant's accrued benefit in optional forms of benefit without complying with specific valuation rules for determining the amount of the distribution. . . .*
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> * * *
>
> (d) Distribution valuation requirements. In determining the present value of any distribution of any accrued benefit from a defined benefit plan, the plan must take into account specified valuation rules. For this purpose, the valuation rules are the same valuation rules for valuing distributions as set forth in section 417(e); see § 1.417(e)-1(d) . . . *This paragraph also applies whether or not the participant's consent is required under paragraphs (b) and (c) of this section.*

26 C.F.R. § 1.411(a)-11 (emphasis added). The "rules for valuing distributions as set forth in section 417(e)," which are incorporated into Treasury Regulation 1.411(a)-11(d), are the same ones set forth in ERISA § 203(e) as interpreted in Treasury Regulation 1.417(e)-1(d).[15] Those valuation rules include this one: "The present value of any optional form of benefit cannot be less than the present value of the normal retirement benefit. . . ." Treas. Reg. § 1.417(e)-1(d). Thus, Treasury Regulation 1.411(a)-11(d) clearly provides that ERISA § 203(e), and the discount interest rates it prescribes, applies to consensual as well as non-consensual lump sum

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[15] To avoid further complicating an already complex discussion, hereinafter when we refer to Treasury Regulation 1.411(a)-11, we mean to include, where relevant, the valuation rules that are contained in Treasury Regulation 1.417(e)-1, which are explicitly incorporated by Treasury Regulation 1.411(a)-11.

distributions. That means Georgia-Pacific loses most of the battle involving the threshold liability issue, if this Treasury regulation is valid.[16]

The district court held that the interest rate restrictions set forth in ERISA § 203(e)(2), 29 U.S.C. § 1053(e)(2), apply solely for the purpose of determining whether the participant's consent is required before the accrued benefit may be distributed in the form of a lump sum. That conclusion is due to be affirmed only if we agree with the district court's holding that Treasury Regulation 1.411(a)-11 is invalid to the extent it provides to the contrary. We turn now to the critical issue of whether that Treasury regulation is due deference, and thus is to be upheld, under the *Chevron* doctrine.

B. Chevron Analysis

"The power of an administrative agency to administer a congressionally created . . . program necessarily requires the formulation of policy and the making of rules to fill any gap left, implicitly or explicitly, by Congress." *Chevron, U.S.A., Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837, 843, 104 S.Ct. 2778, 2782, 81 L.Ed.2d 694 (1984) (quoting *Morton v. Ruiz*, 415 U.S. 199, 231, 94 S.Ct. 1055, 1072, 39 L.Ed.2d 270 (1974)). For that and other reasons, agency regulations, like the one at issue here, are to be given deference "unless they are arbitrary, capricious, or manifestly contrary to the statute." *Id.* at 844, 104 S.Ct. at 2782. Bringing the general deference rule home to the ERISA area in particular, this Court has previously recognized that we "owe great deference to the interpretations and regulations of the Pension Benefit Guaranty Corporation ('PBGC'), the Internal Revenue Service ('IRS') and the Department of Labor, which are the administrative agencies responsible for

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[16] Georgia-Pacific has other arguments and defenses, *see infra* Part II. C. & D., but the validity of this regulation is the big issue.

enforcing and interpreting ERISA." *Blessitt v. Retirement Plan for Employees of Dixie Engine Co.*, 848 F.2d 1164, 1167 (11th Cir.1988) (en banc).

In *Chevron*, the Supreme Court explained: "First, always, is the question whether Congress has directly spoken to the precise question at issue. If the intent of Congress is clear, that is the end of the matter; for the court, as well as the agency, must give effect to the unambiguously expressed intent of Congress." *Chevron*, 467 U.S. at 842-43, 104 S.Ct. at 2781. Thus, our first step is to determine whether Congress' intent, as embodied in ERISA § 203(e) at the time of the payout to Lyons in 1993, is clear that the present value interest rate restrictions contained in that legislation are applicable only to involuntary lump sum distributions. If so, then that is "the end of the matter" and the provisions of Treasury Regulation 1.411(a)-11 to the contrary are invalid.

The intent of Congress behind this part of ERISA § 203(e), at least as it existed at the time Lyons received his distribution in 1993, is anything but clear on this issue. Paragraph (1) of ERISA § 203(e) provides that an involuntary lump sum distribution may not be made when the present value of the vested accrued benefit exceeds $3,500. Paragraph (2)(A) begins with the limiting phrase, "For purposes of paragraph (1)," which seems to indicate that the restrictions on calculating present value which follow that introductory language apply only to the calculation of whether the present value exceeds the $3,500 cap on involuntary distributions contained in paragraph (1).[17] But there is a strong contrary indication in paragraph (2) as well.

Clause (i) of paragraph (2)(A) specifies the applicable discount rate to be used "if the vested accrued benefit (using such rate) is not in excess of $25,000," and clause (ii)

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[17] ERISA § 203(e), as it existed at that time, is set out in its entirety *supra* Part II. A.

specifies a different, higher, discount rate to be used "if the vested accrued benefit exceeds $25,000 (as determined under clause (i))." An additional, final sentence of paragraph (2) reiterates that "[i]n no event shall the present value determined under subclause (II) be less than $25,000,"[18] which is an amount higher than the $3,500 cap for non-consensual distributions set forth in paragraph (1). What all of these references to amounts above and below $25,000 mean is that Congress must have had something other than involuntary distributions in mind, because the cap on them was clearly specified in paragraph (1) to be $3,500. If Congress had intended to address only involuntary distributions, it would have used the $3,500 figure in place of the $25,000 figure in all three places in paragraph (2) of ERISA § 203(e). The $25,000 references make sense only in the context of determining lump sum distributions not governed by the $3,500 cap, which is to say consensual ones.

Georgia-Pacific has never explained why, if ERISA § 203(e) applies only to non-consensual distributions, subparagraph (2) is replete with references to distribution amounts that can only be made with consent. Instead, Georgia-Pacific places great emphasis on the introductory clause ("For purposes of paragraph (1) . . ."), and it also points out that Congress did not change the heading of § 203(e)—"Restrictions on mandatory distributions"—when it made the 1986 amendments to that subsection of ERISA. We have previously observed that "reliance upon headings to determine the meaning of a statute is not a favored method of statutory construction." *Scarborough v. Office of Personnel Management*, 723 F.2d 801, 811 (11th Cir.1984). While section titles or headings may sometimes be useful to resolve

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[18] Everyone agrees that the reference to "subclause (II)" is a typographical error, and that the reference intended is to subclause or clause (ii).

ambiguity in a statute, the ambiguity here is extreme—the language of § 203(e) actually conflicts with itself.

Moreover, the heading upon which Georgia-Pacific relies originated in the 1984 legislation, before Congress added to ERISA § 203(e) the provisions in 1986 that caused the conflict. It is true that when Congress amended the subsection in 1986, it did not alter the heading of § 203(e).[19] Congressional inaction regarding an existing title is far too thin a reed to support a construction of a statutory provision that would effectively write out of it the very changes that Congress amended the provision to include. *Cf. Connecticut Nat'l Bank v. Germain*, 503 U.S. 249, 253, 112 S.Ct. 1146, 1149, 117 L.Ed.2d 391 (1992) ("[C]ourts should disfavor interpretations of statutes that render language superfluous . . . ."); *Bouchard Transp. Co. v. Updegraff*, 147 F.3d 1344, 1351 (11th Cir.1998) ("A basic principle of statutory construction is that a statute should not be construed in such a way as to render certain provisions superfluous or insignificant." (quoting *Woodfork v. Marine Cooks & Stewards Union*, 642 F.2d 966, 970-71 (5th Cir. Apr.1981) (internal quotations and citations omitted))).

The fairest statement that can be made about ERISA § 203(e) on its face is that it is ambiguous about the issue before us. There are indications pointing both ways, although it seems to us that the strongest ones point in the direction of

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[19] However, later that year, the heading of ERISA § 203(e) was changed by the Office of the Law Revision Counsel. *See generally* 2 U.S.C. § 285b(4) (authorizing the Office of the Law Revision Counsel "[t]o classify newly enacted provisions of law to their proper positions in the [United States] Code where the titles involved have not yet been enacted into positive law"). The new heading for ERISA § 203(e), as it appeared in the Code from 1986 to 1994, was: "Consent for distribution; present value; covered distributions." That heading, of course, is less favorable to Georgia-Pacific's position than the one contained in the 1984 version of the legislation.

ERISA § 203(e)'s present value restrictions applying to consensual as well as non-consensual lump sum distributions. Even if we view the ambiguity needle as pointing straight up, the Supreme Court has instructed us:

> [I]f a statute is silent or ambiguous with respect to the question at issue, our longstanding practice is to defer to the executive department's construction of a statutory scheme it is entrusted to administer, unless the legislative history of the enactment shows with sufficient clarity that the agency construction is contrary to the will of Congress.

Japan Whaling Ass'n v. Am. Cetacean Soc'y, 478 U.S. 221, 233, 106 S.Ct. 2860, 2868, 92 L.Ed.2d 166 (1986) (internal quotations and citations omitted).

In the Retirement Protection Act of 1994, Congress removed the language relating to the calculation of present value amounts in excess of $25,000, thereby lessening (or perhaps removing) the ambiguity or self-contradictory nature of the § 203(e) provisions. That amendment may or may not compel a different conclusion as to lump sum distributions made after the effective date of the 1994 legislation. However, Lyons received his distribution in 1993 and the legal issues relating to that distribution, including the validity of Treasury Regulation 1.411(a)-11, are to be decided in view of the statute as it existed at that time.

Georgia-Pacific argues that in the 1994 legislation Congress simply "clarified" its earlier intent. Of course, the Retirement Protection Act of 1994 was enacted by a different Congress than the one that enacted the Tax Reform Act of 1986, which put in place the version of ERISA § 203(e) that we are interpreting. *See Russello v. United States*, 464 U.S. 16, 26, 104 S.Ct. 296, 302, 78 L.Ed.2d 17 (1983)("[I]t is well settled that the views of a subsequent Congress form a hazardous basis for inferring the intent of an earlier one.")

(internal quotations and citations omitted). Whatever effect the 1994 legislation may have on the issues as they relate to distributions after it was enacted, it does not affect our conclusion relating to the issues pertaining to distributions that occurred before then.

Because the language of ERISA § 203(e) itself is ambiguous, at least as it existed at the time Lyons received his distribution, we turn now to the legislative history to see if it "shows with sufficient clarity that the agency construction is contrary to the will of Congress." *Japan Whaling*, 478 U.S. at 233, 106 S.Ct. at 2868. Both parties cite to numerous statements found in the congressional record to support their respective positions. Lyons argues that statements found in the House Conference Report to the Tax Reform Act of 1986 confirm that Congress intended ERISA § 203(e)(2) to apply to all lump sum distributions.[20] That is the legislation that created the textual conflict to begin with.

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[20] The House Conference Report to the Tax Reform Act of 1986 stated:

> If the present value of the vested accrued benefit is no more than $25,000, then the amount to be distributed to the participant or beneficiary is calculated using the PBGC rate.
>
> If the present value of the accrued benefit exceeds $25,000 (using the PBGC interest rate), then the conference agreement provides that the amount to be distributed is determined using an interest rate no greater than 120 percent of the interest rate . . . In no event, however, is the amount to be distributed reduced below $25,000 when the interest rate used is 120 percent of the applicable PBGC rate.
>
> For example, assume that, upon separation from service, the present value of an employee's total accrued benefit . . . is $50,000 using the applicable PBGC rate. Under the conference agreement, the plan may distribute to this employee (if the employee and, if applicable, the employee's spouse consents) the total accrued benefit, calculated using 120 percent of the applicable PBGC rate (e.g., $47,000).

H.R. Conf. Rep. No. 98-841 (1986), *reprinted in* 1986 U.S.C.C.A.N. 4075, 4576. Lyons argues that if the interest rate restrictions applied

Labeling the 1986 legislative history itself "ambiguous," Georgia-Pacific prefers to direct our attention to statements found in the Senate Report to the 1984 legislation which first put ERISA § 203(e) on the books. Georgia-Pacific argues that earlier legislative history shows the discounting-to-present value methodology is limited to involuntary cash-outs of employee benefits.[21] The problem with that argument is that we are concerned with ERISA § 203(e), as amended by the 1986 legislation, not as it existed before. Georgia-Pacific also argues that Congress would have clarified § 203(e) in the Tax Reform Act of 1986 if it had wanted the provision to apply to consensual distributions as well as non-consensual ones. But the same can be said in the other direction: If Congress had wanted § 203(e) to apply only to non-

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solely to the consent determination, the Conference Committee would not have stated that (1) the minimum distribution under the 120% rate is $25,000; and (2) if the amount computed utilizing the 120% rate is, for example, $47,000, the plan must distribute at least $47,000.

[21] The Senate Report to Retirement Equity Act of 1984 states:

> Present Law
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> Under present law, in the case of an employee whose plan participation terminates, a pension, profit-sharing, or stock bonus plan (pension plan) may involuntarily "cash out" the benefit (i.e., pay out the balance to the credit of a plan participant without the participant's consent) if the present value of the benefit does not exceed $1,750 . . . .
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> Reasons for Change
>
> The Committee believes that the limit on involuntary cash-outs should be raised to $3,500 in recognition of the effects of inflation on the value of small benefits payable under a pension plan.
>
> Explanation of Provisions.
>
> The bill provides that, if the present value of an accrued benefit exceeds $3,500, then the benefit is not to be considered non-forfeitable if the plan provides that the present value of the benefit can be immediately distributed without the consent of the participant . . . .

S. Rep. No. 98-575 (1984), *reprinted in* 1984 U.S.C.C.A.N. 2547, 2569.

consensual distributions, it could have clarified the provision in the Tax Reform Act of 1986 to so provide.

As the previous discussion indicates, the legislative history of § 203(e) provides no answer, much less a clear answer, to the issue at hand. Like the language of the provision, the legislative history is ambiguous. As a result, this is a prototypical situation where regulations are permissible, provided they are otherwise reasonable. We turn now to Georgia-Pacific's arguments that Treasury Regulation 1.411(a)-11 is unreasonable.

Georgia-Pacific contends that the Treasury regulation is unreasonable because, all other factors being equal, it produces benefits that are inversely proportional to the age of the participant at the time the lump sum distribution is taken. To the extent that the argument means the earlier a participant leaves employment the better the payout, that is not entirely true. While interest credits continue after separation from employment, service credits do not. The longer a participant stays employed under the Plan, the more service credits will be added to the accrued annuity, and the larger the effect the interest credit will have (because the interest credit is applied to the Personal Account balance which will grow with the addition of service credits). Moreover, those who design plans can reduce any perceived disparity by reducing or eliminating the difference between the statutory discount rate (which was derived from the PBGC rate at the time of Lyons' distribution) and the interest credit rate. To the extent that Treasury Regulation 1.411(a)-11 does make it easier for younger employees to leave an employer who has a front-loaded, cash balance defined benefit plan, we cannot say that consequence makes the regulation unreasonable in light of the fact that one arguable benefit of such plans is that they allow younger workers to take a larger benefit with them when changing jobs. *See Give Employees Meaningful Information*

When Pensions are Changed to Cash Balance Plans, Says Actuary, PR Newswire, May 7, 1999.[22]

Georgia-Pacific also argues that Treasury Regulation 1.411(a)-11 is unreasonable, because it will not work at all where the credit rate varies in response to some measure of market fluctuations, such as a stock or bond index. As an example, Georgia-Pacific posits a farfetched hypothetical.[23] We note that Georgia-Pacific has not cited any evidence or source indicating that such plans exist, or if they do exist, that they are anything but rare.[24] We will not strike down a

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[22] Georgia-Pacific also contends that the practical effect of Treasury Regulation 1.411(a)-11 will be to cause employers to change plans so that the interest credit rate is no more than the statutorily prescribed maximum discount rate. There is nothing in the record or elsewhere that has been brought to our attention indicating that all or most employers will do so, nor are we prepared to say that if that were the effect it would make the regulation unreasonable in the *Chevron* sense.

[23] Georgia-Pacific points out that the S & P 500 gained approximately 28% in 1998, and posits that "[i]f future interest credits were based on the index, Lyons would be entitled to a 28% annual interest credit on his account balance until age 65 which then would be discounted by the PBGC rate (around 5%)." That would produce, Georgia-Pacific says, "a difference of hundreds of thousands (if not millions) of dollars between the actual account balance" and the one due under Lyons' theory. The hypothetical is farfetched, because it would be foolhardy for a plan to base future annual interest credits on any single year's performance of a market index or indicator. If the plan did, the normal retirement benefit under it could be thrown way out of whack, too, even if there were no early lump sum distributions.

[24] Lyons responds to this argument of Georgia-Pacific by suggesting that such a plan would not satisfy the IRC § 401(a)(25) requirement that pension benefits are to be "definitely determinable" in order for the plan to obtain and maintain qualified status under the Code. We have not had sufficient briefing on whether such a plan would tax qualify for us to be able to decide that issue, nor do we need to do so in order to dispose of the present case. But the existence of the tax qualification issue shows the speculative nature of Georgia-Pacific's hypothetical.

regulation on the basis of a speculative hypothetical. Even if such plans do exist, the Plan before us is not one. We address the reasonableness of the Treasury regulation as it applies to the case before us, involving what we understand to be a not untypical type of front-loaded defined benefit plan with a fixed interest credit rate that permits consensual lump sum distributions before normal retirement age. We have no occasion to decide whether Treasury Regulation 1.411(a)-11 might be unreasonable as applied to a materially different plan, such as one in which the interest credit rate varies with market performance.

Because Congress has not spoken directly to the precise issue, because the legislative history is ambiguous, and because Treasury Regulation 1.411(a)-11 is not unreasonable, at least insofar as it applies to the specific type of plan in this case, Treasury Regulation 1.411(a)-11 is due to be upheld under the *Chevron* decision. *See Atlantic Mut. Ins. Co. v. Comm'r*, 523 U.S. 382, 389, 118 S.Ct. 1413, 1418, 140 L.Ed.2d 542 (1998) ("The task that confronts us is to decide, not whether the Treasury regulation represents the best interpretation of the statute, but whether it represents a reasonable one." (citation omitted)); *Chevron*, 467 U.S. at 843 n. 11, 104 S.Ct. at 2782 n. 11 ("The court need not conclude that the agency construction was the only one it permissibly could have adopted to uphold the construction, or even the reading the court would have reached if the question initially had arisen in a judicial proceeding.") We turn now to Georgia-Pacific's contention that even if the Treasury regulation is valid, it does not apply to this specific Plan.

C. Application to the Plan

Lyons argues that Georgia-Pacific violated Treasury Regulation 1.411(a)-11 by failing to project the amount in his hypothetical account to normal retirement age and then discount that figure back to present value using the maximum

discount rate prescribed in ERISA § 203(e)(2). Three years after Lyons received his lump sum distribution, the IRS issued Notice 96-8, which required ERISA plans to do exactly what Lyons argues Georgia-Pacific was required to do at the time it distributed his lump sum benefit to him. *See* I.R.S. Notice 96-8, 1996-1 C.B. 359, 1996 WL 17901. IRS Notice 96-8 definitively states that the discounting-to-present value methodology found in IRC §§ 411 and 417 applies to cash balance plans. The notice explains that when calculating the lump sum distribution under a cash balance plan, "the balance of the employee's hypothetical account must be projected to normal retirement age and then the employee must be paid at least the present value, determined in accordance with [IRC] section 417(e) [one of the tax counterparts to ERISA § 203(e)], of that projected hypothetical account balance." I.R.S. Notice 96-8 (material in brackets added).[25]

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[25] IRS Notice 96-8 states that it was issued to provide "guidance concerning the requirements of section 411(a) and 417(e) with respect to the determination of the amount of a single sum distribution from a cash balance plan." *Id.* It advises that "in order to comply with 411(a) and 417(e) in calculating the amount of a single sum distribution under a cash balance plan, the balance of the employee's hypothetical account must be projected to normal retirement age and then the employee must be paid at least the present value, determined in accordance with section 417(e), of that projected hypothetical account balance." *Id.*

Notice 96-8 explains that if a plan's interest credit rate exceeds the statutory discount rates set forth in IRC § 417(e), then payment of the participant's hypothetical account balance as the lump sum will result in a smaller benefit than the employee is entitled and thereby violate the anti-forfeiture rules in IRC § 411(a) and the present value requirements of IRC § 417(e). The Notice also predicts that anticipated Treasury regulations will contain a list of interest credit rates described as "standard indices and associated margins." Those rates are "assumed" not to exceed the Internal Revenue Code § 417(e) rate, and plans that utilize the proposed interest credit rates may distribute the hypothetical account balance without violating IRC § 417(e). The Notice concludes with a subsection entitled

Georgia-Pacific cannot be held accountable to Lyons for failing to comply with IRS Notice 96-8 per se, because it was released on January 18, 1996, which was *after* Lyons and those similarly situated to him had received their lump sum benefits. A distribution ought to be judged in light of the law and any official guidance that existed at the time of the distribution. Moreover, according to IRS Notice 96-8 itself, its purpose was not to promulgate binding rules, but to elicit opinions on "anticipated regulations."

Georgia-Pacific contends that until IRS Notice 96-8 was issued, there was no guidance suggesting that Treasury Regulation 1.417 would apply to cash balance plans in the manner advocated by Lyons. It argues that even if this Court gives deference to the Treasury regulation, there was no indication at the time of Lyons' lump sum distribution that Georgia-Pacific should have projected the amount in Lyons' hypothetical account to normal retirement age and then discounted that amount back to present value using ERISA § 203(e)(2) and IRC § 417(e) rates.[26] Georgia-Pacific says

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"Guidance will be prospective," which provides a safe harbor for plans that rely on a "reasonable, good-faith interpretation of the applicable provisions of the [Internal Revenue] Code, taking into account pre-existing guidance." *Id.*

[26] Georgia-Pacific's contention disregards a Treasury decision issued well before Lyons received his distribution. On September 19, 1991, the Secretary of the Treasury issued Treasury Decision 8360 which, among other things, stated that cash balance plans must comply with IRC § 417(e) valuation rules even if the resulting lump sum amount would be greater than the amount in the participant's hypothetical account. That Treasury Decision 8360 stated:

> Several commentators requested clarification of the treatment of cash balance plans, another hybrid plan design . . . . Comments indicated that cash balance plans are becoming increasingly popular.
>
> * * *

that until IRS Notice 96-8 all it was required to distribute as a lump sum was the amount in an individual employee's hypothetical account.[27] We are skeptical about whether lack of guidance and direction can be a defense to this type of action by a plan participant, and in any event Treasury Regulation 1.411(a)-11 when read against the Plan's own terms provides enough guidance that Georgia-Pacific is liable

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> Some of the comments involving cash balance plans . . . requested that the final regulations provide special relief for cash balance plans from the requirements of section 417(e) These rates, when combined into a single blended rate, are sometimes lower than the rates used by existing cash balance plans in determining employees' cash balances, and can therefore require a plan that does not use the section 417(e) rates to determine interest adjustments to pay an employee more than the amount of the employee's hypothetical cash balance when benefits are paid in a single sum. The Treasury and the Service have determined that such relief cannot be granted consistent with the requirements of section 417(e). However, in order to minimize the occasions when this problem will arise, the final regulations include a blended section 417(e) interest rate among the alternative safe harbor interest rates a cash balance plan may use in determining interest adjustments.

T.D. 8360, 56 Fed Reg. 47524, 47528 (1991). Thus, the Treasury Department had put employers on notice of its position that the law required cash balance plans to use the statutory rates in IRC § 417(e), at the time Lyons received his payout, to discount to present value the normal retirement benefit that would have been received if an early lump sum distribution had not been elected.

[27] Along these lines, Georgia-Pacific argues that ERISA § 204(c)(2)(C) permitted it to limit the lump sum distribution to Lyons' Personal Account Balance. But ERISA § 204(c)(2)(C) addresses situations involving "accumulated contributions," which are defined as those that include "mandatory contributions made by the employee." 29 U.S.C. § 1054(c)(2)(C)(i). The Plan in this case did not require or permit employee contributions, so the provision Georgia-Pacific relies upon does not apply.

to plan participants even for distributions made before the issuance of IRS Notice 96-8.[28]

Reiterating some of the features of a cash balance plan is helpful in explaining Georgia-Pacific's obligations under the law as it existed at the time of Lyons' lump sum distribution. As we have explained before, a defined benefit, cash balance plan, such as this one, credits a hypothetical account with service credits and interest credits. Nevertheless, as a defined benefit plan, the plan "consists of a general pool of assets rather than individual dedicated accounts." *Hughes Aircraft Co. v. Jacobson*, 525 U.S. 432, 439, 119 S.Ct. 755, 761, 142 L.Ed.2d 881 (1999). In a cash balance type of defined benefit plan, "[t]he total assets on deposit do not generally equal the total of all balances maintained for participants." Brown, *supra* note 1, at 83. "[T]he employer typically bears the entire investment risk and—sort of the consequences of plan termination—must cover any underfunding as the result of a shortfall that may occur from the plan's investments." *Hughes Aircraft Co.*, 525 U.S. at 439, 119 S.Ct. at 761 (citing *Connolly v. Pension Benefit Guaranty Corp.*, 475 U.S. 211, 232, 106 S.Ct. 1018, 89 L.Ed.2d 166 (1986) (O'Connor, J. concurring)).

Because the plan here is a defined benefit plan, the individual employees "have a right to a certain defined level

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[28] IRS Notice 96-8 contains a "safe harbor" clause that protects from tax disqualification a plan in which pre-Notice distributions were made inconsistently with the provisions of the notice "if the amount of the distribution satisfied those [applicable Internal Revenue Code] sections based on a reasonable, good-faith interpretation of the applicable provisions of the Code, taking into account pre-existing guidance." I.R.S. Notice 96-8. It is by no means clear that Georgia-Pacific could meet the requirements of that "safe harbor." *See* discussion of Treasury Decision 8360 *supra* n. 26. Even if Georgia-Pacific could meet those requirements, it would be safely harbored only from tax disqualification, not from liability to plan participants.

of benefits, known as 'accrued benefits.'" *Id.* at 440, 119 S.Ct. at 761. "That term, for purposes of a defined benefit plan, is defined as 'the individual's accrued benefit determined under the plan [and ordinarily is] expressed in the form of an annual benefit commencing at normal retirement age.' " *Id.* (quoting ERISA § 3(23)(A), 29 U.S.C. § 1002(23)(A)).[29] The Plan involved in this case defines "Accrued Benefit" as follows:

> Accrued Benefit means, as of the time of reference, a monthly amount of benefit, payable in the form of an increasing life annuity, commencing on a Participant's Normal Retirement Date, where the amount of such monthly benefit is the result of dividing the then credits to such Participant's Personal Account by the applicable factor from Section A of Appendix A.

Unlike a defined contribution plan, the "accrued benefit" under this Plan is not the amount in the Participant's Personal Account, but rather an amount *derived from* that hypothetical account. Thus, Lyons did not have a statutory right to the amount found in his hypothetical account prior to the normal retirement date, and Georgia-Pacific did not have a right to limit any distribution to him to that amount. Instead, after five years of work, Lyons earned a vested interest in an amount at normal retirement age, to be calculated under the Plan by projecting forward the amount in his hypothetical account using the interest credit rates specified in the Plan.

Treasury Regulation § 1.417(e)-1, which was in effect at the time of the distribution, unequivocally states that "[t]he present value of *any* optional form of benefit cannot be less than the present value of the *normal retirement benefit*

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[29] "By contrast, an 'accrued benefit' for purposes of defined contribution plans means 'the balance of the individual's account.'" *Hughes Aircraft Co.*, 525 U.S. at 440 n. 3, 119 S.Ct. at 761 n. 3 (quoting ERISA § 3(23)(B); 29 U.S.C. § 1002(23)(B)).

determined in accordance with this paragraph." Treas. Reg. § 1.417(e)-1(d) (emphasis added). "Any" means exactly what it says. *See Lyes v. City of Riviera Beach, Florida*, 166 F.3d 1332, 1337 (11th Cir.1999) (en banc) (when no limiting language is used " 'any' means all.") (internal quotations and citations omitted). "[A]ny optional form of benefit" includes a pre-retirement lump sum benefit, which means that such a lump sum distribution cannot be less than "the present value of the normal retirement benefit determined in accordance with" the Treasury regulation.

The "normal retirement benefit" itself, before it is discounted to present value, is determined in accordance with the Plan. It is the amount a participant would have received at age 65 under the Plan but for the election to take an early lump sum distribution. *See* Treas. Reg. § 1.417(e)-1. To determine the normal retirement amount Lyons would have received at age 65, the Plan specifies that his hypothetical account balance must be projected forward using the interest credit rates set forth in the Plan. It is the Plan itself, rather than the Treasury regulations, that requires the hypothetical account balance to be projected forward using the credit interest rate, and it is the Plan itself that specifies the interest credit rate to be applied for that purpose. What the Treasury regulation adds is that once the normal retirement benefit is ascertained in accordance with the Plan, that amount is then to be discounted to present value using the PBGC rate in order to calculate the lump sum distribution to which the participant is entitled.

For these reasons, we conclude that Treasury Regulation 1.411(a)-11, which was issued in 1988, requires that lump sum distributions under the Plan be calculated by determining what would have been the normal retirement benefit had the participant not elected to take an early lump sum distribution, and then discounting that amount to present value using the PBGC rate prescribed in ERISA § 203(e). Distribution of the

hypothetical account balance alone is not enough where, as here, the interest credit rate exceeds the PBGC rate.

D. The IRS Determination Letter

In 1989 the IRS issued Georgia-Pacific a determination letter stating that the Plan was tax qualified. Georgia-Pacific argues that based upon that letter it cannot be held liable for any underpayment of benefits to Lyons and those similarly situated. The reasoning is that in determining the plan was tax qualified the IRS must have concluded that distributing the participant's Personal Account complied with IRC § 417(e), the Internal Revenue Code subsection that parallels ERISA § 203(e).

The one-page determination letter makes no mention at all of the lump sum payment provision, nor is there any indication in the letter that the IRS considered that provision of the Plan, much less the issue now before us. In its amicus brief the IRS urges us not to consider the letter, because it "may have erroneously overlooked the plan provision" for lump sum payments. Because it does not specifically address the issue at hand, the IRS letter is not owed any deference. *See Hickey v. Chicago Truck Drivers, Helpers & Warehouse Workers Union*, 980 F.2d 465, 469 (7th Cir.1992) ("Given the informal nature of these letters, the express limitations included in the IRS letter, and the absence of any reasoning to explain the basis for the statements, we do not think that any implication in either of these letters . . . is entitled to deference."); *In re Gulf Pension Litigation*, 764 F.Supp. 1149, 1172 (S.D.Tex.1991) ("[T]he Court also finds that the IRS determination is due no deference because it evidences no investigation or legal analysis of the facts by the IRS.").

The letter may protect the Plan from adverse tax treatment, but it does not protect the Plan from liability to participants.[30]

E. Class Representative Problems

The Plan in this case was changed to a cash balance defined benefit plan by an amendment that became effective January 1, 1989. Thereafter, and until the Plan was amended in 1997, it utilized an interest credit rate that was higher than the statutorily prescribed maximum discount rate. The class the district court defined covered all of those who had received lump sum distributions under the Plan that were lower than the present value of their accrued retirement benefit would have been if calculated using the statutorily prescribed discount rate.

Lyons, who is currently the only class representative, received his lump sum distribution in January of 1993. The version of ERISA § 203(e) on the books at that time had remained unchanged in any material way since amendments were made to it by the Tax Reform Act of 1986, and that version continued in effect without material change until amended by the Retirement Protection Act of 1994. Thus, from all that appears Lyons is an adequate representative for all class members who received their lump sum distributions before the 1994 amendment took effect.[31] He suffered the

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[30] The same is true of an IRS determination letter Georgia-Pacific received in 1997, after it made amendments to the Plan that are not relevant to the issue in this case. We mention that second letter only in a footnote, because it was issued long after Lyons and those similarly situated with him had received their distributions.

[31] The 1994 legislation specifies that the relevant amendment "shall apply to plan years and limitation years beginning after December 31, 1994; except that an employer may elect to treat the amendments made by this section as being effective on or after the date of enactment of this Act [December 8, 1994]." Retirement Protection Act of 1994, P.L. 103-

same type of injury as they did, and the law applicable to his claim is the same as that applicable to theirs.

However, Lyons is not an adequate representative for those class members who received their lump sum distributions after the effective date of the 1994 amendment, because their claims are governed by ERISA § 203(e) as amended by that legislation. Lyons has no interest in whether the 1994 amendment altered the legal landscape for those who received distributions thereafter. It does not matter to him, for example, whether the amended language is sufficiently free of ambiguity that the *Chevron* analysis may come out differently. *See supra* Part II. B. Even if it does, that will not affect his claim which is governed by pre-1994 law.

As we have explained before:

> Among the prerequisites to the maintenance of a class action is the requirement of Rule 23(a)(4) that the class representatives "will fairly and adequately protect the interests of the class." The purpose of this requirement, as of many other of Rule 23's procedural mandates, is to protect the legal rights of absent class members. Because all members of the class are bound by the res judicata effect of the judgment, a principal factor in determining the appropriateness of class certification is "the forthrightness and vigor with which the representative party can be expected to assert and defend the interests of the members of the class."

Kirkpatrick v. J.C. Bradford & Co., 827 F.2d 718, 726 (11th Cir.1987) (citations omitted). We cannot expect Lyons to assert with "forthrightness and vigor" those interests of other class members that he does not share and in which he has no

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465, § 767(d), 108 Stat. 4809, 5039. *See also* ERISA § 205(g)(3)(B), 29 U.S.C. § 1055(g)(3)(B).

stake. Indifference as well as antagonism can undermine the adequacy of representation.[32]

Because there is no adequate class representative before us to advocate the interests of those who received their lump sum distributions after the effective date of the amendment that the Retirement Protection Act of 1994 made to ERISA § 203(e), we have declined to decide whether Treasury Regulation 1.411(a)-11 is a valid regulation insofar as it concerns those distributions. *See supra* 1246. On remand, if an adequate class representative appears to advocate the interests of those who have a stake in that issue, the district court should proceed to decide that issue, and any other issues concerning the threshold liability question that relate particularly to those class members, in the first instance.

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[32] We realize, of course, that class issues, including those relating to the adequacy of representation requirement, are ordinarily raised in the district court whose rulings on such issues are reviewed only for an abuse of discretion. However, the circumstances here are a bit unusual. The district court held that no class member, including Lyons, was entitled to any relief because Treasury Regulation 1.411(a)-11 was unreasonable and invalid even as it applied to those who received their distributions before the effective date of the 1994 amendment to ERISA § 203(e). Lyons appears to have been an adequate representative of all those in the class as to that issue. But now that we have reversed the district court's holding, the issue concerning the adequacy of representation involving distributions made after the 1994 amendment arises. Adequacy of representation issues implicate due process, *see In re Am. Med. Sys., Inc.*, 75 F.3d 1069, 1083 (6th Cir.1996), and may be addressed throughout the litigation, *see Barney v. Holzer Clinic, Ltd.*, 110 F.3d 1207, 1213-14 (6th Cir.1997)(court of appeals *sua sponte* narrowing class definition and limiting judgment accordingly); *cf.* 7A Charles Alan Wright & Arthur R. Miller, Federal Practice and Procedure § 1765, at 293 (2d ed. 1986) ("[A] favorable decision under Rule 23(a)(4) is not immutable. If later events demonstrate that the representatives are not adequately protecting the absentees, the court may take whatever steps it thinks necessary under Rule 23(c) or Rule 23(d) at that time.")

III. CONCLUSION

Treasury Regulation 1.411(a)-11 is a reasonable and valid interpretation of ERISA § 203(e), as it existed prior to its amendment by the Retirement Protection Act of 1994, at least as that provision applies to defined benefit cash balance plans with fixed interest credit rates. The district court's judgment, which is based on a holding to the contrary, is due to be reversed.[33]

REVERSED and REMANDED for further proceedings consistent with this opinion.

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[33] As we mentioned earlier in this opinion, the district court at the urging of the parties addressed only the threshold liability issue of potential liability to any class member, and left for the future discovery and decision of other issues that might arise if potential liability were found. *See supra* Part I.C. We leave those issues and any additional defenses Georgia-Pacific may have that are not inconsistent with our holdings in this opinion to be decided on remand.

APPENDIX B

UNITED STATES DISTRICT COURT
N.D. GEORGIA
ATLANTA DIVISION

No. Civ.A.1:97CV0980-JOF

JERRY L. LYONS, individually and on behalf of all others similarly situated,

Plaintiff,

v.

GEORGIA-PACIFIC CORPORATION SALARIED EMPLOYEES RETIREMENT PLAN AND GEORGIA-PACIFIC CORPORATION,

Defendants.

March 22, 1999

ORDER

FORRESTER, District Judge.

This matter is before the court on Defendants' motion for summary judgment [22-1] and Plaintiff's cross motion for summary judgment [23-1].

I. STATEMENT OF THE CASE

Plaintiff Jerry L. Lyons filed the instant action on behalf of himself and a class of persons similarly situated against Defendants Georgia-Pacific Corporation and Georgia-Pacific Corporation Salaried Employees Retirement Plan ("SERP" or the "Plan") pursuant to the Employment Retirement Income Security Act of 1974 ("ERISA"), 29 U.S.C. § 1001, *et seq.*, alleging that he was denied his proper benefits under the Plan.

He claims that under § 502(a)(3) of ERISA he is entitled to bring an action to enjoin Defendants' violation of the statute and to obtain equitable relief. The dispute in this case arises over the statutory interpretation of ERISA in conjunction with various provisions of the Internal Revenue Code ("IRC" or "Code") and Treasury Regulations promulgated thereunder. Both Plaintiff and Defendants have filed motions for summary judgment. The parties participated in oral argument before the undersigned on March 11, 1999.

The following facts are undisputed.[1] Plaintiff is a former employee of Defendant Georgia-Pacific Corporation and was a participant in the Defendant SERP. The Plan was a cash balance defined benefit plan, which is a pension plan that defines retirement benefits for employees by reference to a hypothetical account to which hypothetical contributions are periodically made pursuant to various formulas set forth in the Plan. The Plan provided participants with individual account statements of their hypothetical account balances and allowed participants to elect to receive a lump sum distribution of benefits under the Plan in the amount of the balance of their hypothetical accounts.

Plaintiff's employment with Georgia-Pacific terminated on January 5, 1991. At that time, he was 49 years old and had completed over five years of service and was therefore eligible for a "vested" benefit under the Plan. In 1993, Plaintiff elected to receive a total lump sum distribution of his SERP benefits. In accordance with the provisions of the Plan, he received the amount stated as the balance of his individual account: $36,109.35. Although the lump sum distribution made to Plaintiff complied with the terms of the SERP, Plaintiff contends that it was in violation of ERISA.

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[1] The undisputed facts are taken from both parties' motions for summary judgment and construed pursuant to Local Rule 56.1B(2).

Since the commencement of the instant action, the parties have agreed to certification of a class of those employees similarly situated to Plaintiff. Pursuant to a stipulation agreed to by the parties, the court entered an Order certifying a class pursuant to Fed.R.Civ.P. 23(a) of:

> All participants (or beneficiaries of participants) in the [Plan] (i) who received a lump sum distribution of benefits calculated at a time when such participants had a vested interest in the Plan and who (ii) received a distribution of benefits in a lump sum where (iii) at the date as of which the amount of the lump sum was calculated, the lump sum was lower than the present value, if determined using the "applicable interest rate" as defined in Internal Revenue Code Section 417(e)(3) and set forth in Treasury Regulations issued pursuant to Internal Revenue Code Section 417(e), of such participants' accrued benefit, as defined under ERISA.

(Order, September 19, 1997).

The Plan

Taken from the documents submitted by both parties, the court finds the following terms of the SERP relevant. The Plan provided a "Personal Account" to be established for each Participant under the Plan, and for basic monthly credits to be made to the Personal Account for service, depending upon the Participant's compensation. (Plan §§ 3.1, 3.2). Specifically, "[t]he amount of monthly credits to the Personal Account of an eligible Participant [was] equal to four percent (4%) of the Participant's Compensation for that calendar month as determined by the Plan Administrator." (Plan § 3.2). Monthly credits were to be issued to the accounts only up until the Participant's "Severance Date." The Plan went on to provide "Additional Credits" to be issued depending upon the Participant's age at the time of the Plan's effective date (§ 3.3), as well as "Periodic Adjustments" (§ 3.5). Each

Participant's Personal Account was to be automatically increased at the end of each month by Periodic Adjustment Percentage ("PAP"). The PAP was calculated as follows:

> (1) Determine the PBGC [Pension Benefit Guaranty Corporation] 12 month average immediate annuity interest rate for the calendar year preceding the year in which the adjustment is to be made;
>
> (2) Add to (1).75%;
>
> (3) Divide the sum of (1) and (2) by 12; and
>
> (4) Round the result to 6 decimal places.

(Plan § 3.5). Each account was to be increased by an amount equal to the product of the PAP and the Personal Account balance at the beginning of the month up until the Benefit Commencement Date.

The Plan provided five forms of retirement benefits: Normal retirement, early retirement, postponed retirement, disability retirement, and vested benefit. (Plan §§ 4.1-4.5). Normal Retirement was available for a Participant who terminated employment on the Normal Retirement Date. (Plan § 4.1). Normal Retirement Date was defined in the Plan as a Participant's 65th birthday. (Plan § 1.29). A "Vested Benefit" was defined as available for those Participants not eligible for the remaining four retirement benefits who terminated employment after at least five years of service. (Plan § 4.5). The Plan defined the vested benefit for a participant as "equal to his then Accrued Benefit payable in accordance with the provisions of Article 6" of the Plan. (*Id.*). It appears that the normal form of benefit is an increasing annuity.

Further, the Plan provided optional forms of benefits, allowing a Participant to receive, in lieu of the standard benefit, several alternate forms of payment. One of these options was "a single lump sum payment equal to the amount credited to the Participant's Personal Account as of the end of

the month preceding his Benefit Commencement Date." (Plan § 6.4).

The Benefit Commencement Date under the Plan was defined as:

> in the case of an annuity form of distribution, the first day of the first period for which an amount is payable as an annuity under this Plan and, in the case of a lump sum payment, the first date on which all events have occurred which entitle the Participant to payment under this Plan.

(Plan § 1.5).

Applicable Statutes and Treasury Regulations

At the time the distribution at issue in this case was made to Plaintiff, section 203(e) of ERISA provided:

(e) Consent for distribution; present value; covered distributions

(1) If the present value of any nonforfeitable benefit with respect to a participant in a plan exceeds $3,500, the plan shall provide that such benefit may not be immediately distributed without the consent of the participant.

(2)(A) For purposes of paragraph (1), the present value shall be calculated—

(i) by using an interest rate no greater than the applicable interest rate if the vested accrued benefit (using such rate) is not in excess of $25,000, and

(ii) by using an interest rate no greater than 120 percent of the applicable interest rate if the vested accrued benefit exceeds $25,000 (as determined under clause (i)).

In no event shall the present value determined under subclause (II)[sic] be less than $25,000.

(B) For purposes of subparagraph (A), the term "applicable interest rate" means the interest rate which would be used (as of the date of the distribution) by the Pension Benefit Guaranty Corporation for purposes of determining the present value of a lump sum distribution on plan termination.

ERISA § 203(e), 29 U.S.C. § 1053(e).[2] [3]

Section 3002 of ERISA provides for "procedures with respect to continued compliance with Internal Revenue requirements relating to participation, vesting, and funding standards." Specifically, § 3002(c) states:

> Regulations prescribed by the Secretary of the Treasury under sections 410(a), 411 and 412 of Title 26 (related to minimum participation standards, minimum vesting standards, and minimum funding standards, respectively) shall also apply to the minimum participation, vesting and funding standards set forth in parts 2 and 3 of subtitle B of subchapter I of this chapter.

ERISA § 3002(c), 29 U.S.C. § 1202(c).

The means for calculating the amount of the lump sum payment urged by the Plaintiff does not expressly appear in ERISA § 203(e). It does appear in Treasury Regulation § 1.411(a)-11, promulgated under IRC § 411, which provides for "restriction and valuation of distributions" and states:

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[2] ERISA § 203(e)(2) 29 U.S.C. § 1053(e)(2) was amended in 1994 to provide an alternate formula for calculation of present value in accordance with 29 U.S.C. § 1055(g)(3), which determines present value by reference to the applicable mortality table and applicable interest rate. All references in this Order to ERISA § 203(e) refer to the pre-1994 version.

[3] At the time Plaintiff received his distribution in the instant case, IRC § 417(e)(3) contained language identical to that of § 203(e)(2) of ERISA in defining the determination of present value.

> Section 411(a)(11) restricts the ability of a plan to distribute any portion of a participant's accrued benefit without the participant's consent. *Section 411(a)(11) also restricts the ability of defined benefit plans to distribute any portion of a participant's accrued benefit in optional forms of benefit without complying with specified valuation rules for determining the amount of the distribution.* If the consent requirements or the valuation rules of this section are not satisfied, the plan fails to satisfy the requirements of section 411(a).

(Emphasis supplied). Treas.Reg. § 1.411(a)-11(a)(1); 26 C.F.R. § 1.411(a)-11(a)(1). Section 1.411(a)-11(d) then went on to discuss these "distribution valuation requirements" and stated, "[i]n determining the present value of any distribution of any accrued benefit from a defined benefit plan, the plan must take into account specified valuation rules. For this purpose, the valuation rules are the same valuation rules for valuing distributions as set forth in section 417(e); *see* § 1.417(e)-1(d)." § 1.411(a)-11(d).

At the time relevant to the instant case, Treasury Regulation 1.417(e)-1(d), promulgated under IRC § 417(e), provided:

> *Present value requirement—(1) Requirements.* For purposes of determining the present value of any accrued benefit and for purposes of determining the amount (subject to sections 411(c)(3) and 415) of any distribution including a single sum, a defined benefit plan is subject to the interest rate limitations described in subparagraph (2) of this paragraph (d) at the time set forth in paragraph (3) of this paragraph (d). A plan amendment that changes the rate described in this paragraph (d) is subject to section 411(d)(6). *The present value of any optional form of benefit cannot be less than the present value of the normal retirement benefit determined in accordance with this paragraph.*

* * *

(Emphasis supplied).[4] Treas.Reg. § 1.417(e)-1(d); 26 C.F.R. § 1.417(e)-1(d).[5]

The Parties' Contentions

Reading the above-referenced statutes and regulations together, Plaintiff contends that Defendants were required, when determining the amount of his benefits, to give effect to Treas.Reg. §§ 1.417(e)-1(d) and 1.411(a)-11, as incorporated into ERISA through § 3002(c). Plaintiff therefore concludes that Defendants should have calculated the present value of his normal retirement benefit under the formula provided in ERISA § 203(e)(2) and paid him no less than that amount. Plaintiff claims that he was entitled to $49,341.83 instead of the $36,109.15 he received under the Plan.

Defendants contend that Plaintiff cannot rely on ERISA § 203(e) in this case, because by its terms it only applies to involuntary distributions and the distribution in this case was voluntarily received by Plaintiff. Defendants base their position on the language of § 203(e), which sets forth the formula for calculating present value and specifically limits the use of the formula to the "purposes of paragraph (1)." ERISA § 203(e)(2). Defendants assert that because

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[4] On January 18, 1996, the IRS released Notice 96-8, 1996-1 C.B. 359, for the purpose of providing "guidance concerning the requirements of section 411(a) and 417(e) with respect to the determination of the amount of a single sum distribution from a cash balance plan." 1996-1 C.B. at 1. After a brief description of cash balance plans as a type of defined benefit pension plan, the Service stated, "in order to comply with 411(a) and 417(e) in calculating the amount of a single sum distribution under a cash balance plan, the balance of the employee's hypothetical account must be projected to normal retirement age and then the employee must be paid at least the present value, determined in accordance with section 417(e), of that projected hypothetical account balance." *Id.* at 2.

[5] Treas.Reg. § 1.417(e)-1 has currently been amended. All references in this Order to the regulation refer to the pre-1994 version.

paragraph (1) of § 203(e) is directed toward a determination of whether consent is required for immediate distribution, the provision and its formula for present value are inapplicable in the instant case.

Plaintiff cites in response to Defendants' argument the Treasury Regulations promulgated under IRC § 411, made applicable to ERISA through § 3002(c), which explain that "[i]n determining the present value of any distribution of any accrued benefit from a defined benefit plan, the plan must take into account specified valuation rules," and also that the provision "applies whether or not the participant's consent is required. . . ." Treas.Reg. § 1.411(a)-11(d). The valuation rules referenced in Treas.Reg. § 1.411(a)-11(d) are those set forth in Treas.Reg. § 1.417(e)-1(d), which state, "[t]he present value of any optional form of benefit cannot be less that the present value of the normal retirement benefit. . . ." Treas.Reg. § 1.417(e)-1(d). Through these regulations, Plaintiff finds authority for his cause of action under ERISA § 203(e).

II. DISCUSSION

Resolution of the dispute between the parties as to the applicability of § 203(e) of ERISA turns on a determination of whether the Treasury Regulations promulgated under the Internal Revenue Code can be relied upon to create a substantive right under ERISA in the instant case. In general, courts do not incorporate Treasury Regulations into ERISA to create substantive rights. *See, e.g., Tulley v. Ethyl Corp.*, 861 F.2d 120, 125 (5th Cir.1988); *Dooley v. American Airlines, Inc.*, 797 F.2d 1447, 1452-53 (7th Cir.1986) (refusing to incorporate regulations promulgated under IRC § 401 into ERISA and citing as authority ERISA § 3002(c), 29 U.S.C. § 1202(c)); *Reklau v. Merchants Nat. Corp.*, 808 F.2d 628, 630-31 (7th Cir.1986) (rejecting contention that regulations promulgated under IRC § 401 can be made applicable to ERISA under ERISA § 3002(c), 29 U.S.C. § 1202(c), and

also finding that IRC § 401 cannot create substantive rights under ERISA); *Cowan v. Keystone Emp. Profit Sharing Fund*, 586 F.2d 888, 890, n. 3 (1st Cir.1978) (finding no substantive right created under IRC § 401).

However, certain regulations promulgated under IRC §§ 410(a), 411 and 412 have been specifically incorporated into ERISA under § 3002(c). Courts have recognized that Treasury Regulations promulgated under these code sections are equally applicable to certain provisions of ERISA. *See, e.g., Williams v. Cordis Corp.*, 30 F.3d 1429, 1431, n. 2 (11th Cir.1994); *Counts v. Kissack Water and Oil Serv., Inc.*, 986 F.2d 1322, 1324, n. 1 (10th Cir.1993); *Abraham v. Exxon Corp.*, 85 F.3d 1126, 1131 (5th Cir.1996). Further, regulations promulgated under ERISA explain the close relationship between specific provisions of ERISA and the Internal Revenue Code. 29 C.F.R. § 2530.200a-1 (stating that the requirements of Part 2 of Title I of ERISA, which contains minimum standards that an employee pension benefit plan must satisfy, are "substantially identical" to the requirements of Subchapter D of Chapter 1 of Subtitle A of the Internal Revenue Code, which sets forth standards for plans seeking qualification for certain tax benefits). Specifically, the regulations under ERISA state:

> Regulations prescribed by the Secretary of the Treasury or his delegate under sections 410 and 411 of the Code (relating to minimum standards for participation and vesting) shall apply for purposes of sections 202 through 204 of [ERISA]. Thus, except for those provisions . . . for which authority to prescribe regulations is specifically delegated to the Secretary of Labor, regulations prescribed by the Secretary of the Treasury shall also be used to implement the related provisions contained in [ERISA].

29 C.F.R. § 2530.200a-2.

Under this authority, the court will construe Treasury Regulation § 1.411 as incorporated into ERISA § 203, as IRC § 411 is the statutory analog to ERISA § 203. However, the substantive right asserted by Plaintiff in the instant case does not appear on the face of the ERISA statute. The appropriate inquiry thus becomes whether the authority to create the substantive right under ERISA at issue in this case was properly delegated by Congress to the Secretary of Treasury and consequently whether the regulation can be given force and effect.

Both IRC § 411 and ERISA § 203 set forth "minimum vesting standards" and specifically require that qualified plans provide that "an employee's right to his normal retirement benefit is nonforfeitable upon the attainment of normal retirement age." IRC § 411(a); ERISA § 203(a). Both statutes also go on to require in substantially similar language that if the "present value" of any participant's vested and nonforfeitable benefit exceeds $3,500, the plan must provide that such benefit may not be immediately distributed without the consent of the participant. IRC § 411(a)(11)(A); ERISA § 203(e)(1). The statutes then set forth, *for purposes of* the requirements in IRC § 411(a)(11)(A) and ERISA § 203(e)(1), identical formulas for the computation of present value.[6] IRC § 411(a)(11)(B); ERISA § 203(e)(2).

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[6] The present value is calculated:

> (I) by using an interest rate no greater than the applicable interest rate if the vested accrued benefit (using such rate) is not in excess of $25,000, and
>
> (II) by using an interest rate no greater than 120 percent of the applicable interest rate if the vested accrued benefit exceeds $25,000 (as determined under clause (I)). In no event shall the present value determined under subclause (II) be less than $25,000.

IRC § 411(a)(11)(B); ERISA § 203(e)(2).

The Treasury Regulations promulgated under IRC § 411 specifically address § 411(a)(11). In describing the scope of the statute, the regulations explain that § 411(a)(11) restricts the ability of a plan to distribute an accrued benefit without the consent of the participant, and go on to state that "[s]ection 411(a)(11) also restricts the ability of defined benefit plans to distribute any portion of a participant's accrued benefit in optional forms of benefit without complying with specified valuation rules for determining the amount of the distribution." Treas.Reg. § 1.411(a)-11(a)(1). Section 1.411(a)-11(d) discusses these "distribution valuation requirements," referring to the valuation rules set forth in IRC § 417(e) and Treasury Regulation § 1.417(e)-1(d).

Applying these regulations to ERISA, the court finds that the terms of Treas.Reg. § 1.411(a)-11 would require a plan to comply with the valuation rules set forth in Treas.Reg. § 1.417(e)-1(d) before distributing any portion of a participant's benefit in an optional form. Specifically, the regulations would direct that under ERISA, "[t]he present value of any optional form of benefit cannot be less than the present value of the normal retirement benefit determined in accordance with this paragraph." Treas.Reg. § 1.417(e)-1(d). Accordingly, the application of these regulations would require a plan, in order to comply with ERISA, to make a present value calculation of a participant's normal retirement benefit in accordance with the formula under ERISA § 203(e)(2) and distribute no less than that amount as the present value of an optional benefit.

ERISA § 203(e) on its face applies only in the context of determining whether consent of a participant is required as a prerequisite to making an immediate distribution of benefits. The regulations discussed above necessarily expand the application of § 203(e) to all distributions of benefits, regardless of whether or not consent is required for the distribution. To determine whether application of these

regulations to ERISA can be considered supported by a proper delegation under ERISA to the Secretary of Treasury, the court turns to the guidance of the Supreme Court as set forth in *Chevron U.S.A., Inc. v. Natural Resources Defense Council, Inc.*, 467 U.S. 837, 104 S.Ct. 2778, 81 L.Ed.2d 694 (1984). *Chevron* requires a two-pronged analysis of an agency's interpretation of a statute: (1) "whether Congress has directly spoken to the precise question at issue," and, if not, (2) "whether the agency's answer is based on a permissible construction of the statute." 467 U.S. at 842-43, 104 S.Ct. 2778. Where Congress clearly leaves a gap to be filled by an administrative agency, there is an "express delegation" of authority, and regulations enacted thereunder are "given controlling weight unless they are arbitrary, capricious, or manifestly contrary to the statute." *Id.* at 844, 104 S.Ct. 2778. Legislative delegation to an agency can also be implicit rather than explicit, and in that case "considerable weight should be accorded to an executive department's construction of a statutory scheme it is entrusted to administer." *Id.* at 844, 104 S.Ct. 2778. The question for the court in this latter situation is whether the agency's interpretation was a "reasonable" one. *Id.* at 845, 104 S.Ct. 2778.

Congress has generally delegated to the Secretary of Treasury the task of administering the nation's tax laws under 26 U.S.C. § 7805, which provides that "the Secretary shall prescribe all needful rules and regulations for the enforcement" of the Code. Although particular deference is shown by courts in the area of tax law, a regulation deemed unreasonable will not be given force and effect. *United States v. Cartwright*, 411 U.S. 546, 550, 93 S.Ct. 1713, 36 L.Ed.2d 528 (1973), *R.J.R. Nabisco, Inc. v. United States*, 955 F.2d 1457, 1464 (11th Cir.1992); *Chevron*, 467 U.S. at 845, 104 S.Ct. 2778.

As discussed below, the court cannot find that the Secretary of Treasury's interpretation of ERISA § 203(e) through Treasury Regulation § 1.411(a)-11 was a reasonable one that can be given force and effect in the instant case. ERISA § 203 is directed toward the establishment of "minimum vesting standards," and subsection (e) specifically legislates requirements for "consent for distribution; present value; covered distributions." ERISA § 203(e) plainly sets forth requirements for situations in which employers must obtain the consent of participants before making immediate distributions of benefits and provides a formula *for the purpose of* calculating present value in making this determination. ERISA § 203(e). Nowhere on the face of § 203(e) is there any reference to general lump sum distributions under the plan. In addition, the court can find no suggestion in the legislative history or otherwise to suggest that ERISA § 203(e) was intended to serve as a blanket requirement that any distribution under an ERISA plan comply with the formula for present value set forth in § 203(e)(2). Further, even looking beyond ERISA, the court finds no authority in the legislative history of IRC § 411 or otherwise to support the portion of Treas.Reg. § 1.411(a)-11 as applied under the Code. Instead, commentary relating to both ERISA § 203 and IRC § 411 which was considered by the court seems to refer only to the present value computation in the context of determining whether benefit distributions can be involuntarily made. *See, e.g.*, S.Rep. No. 103-412 (1994); H.R.Rep. No. 103-826(I) (1994); H.R.Rep. No. 103-632(I) (1994).

It is evident that Treasury Regulation § 1.411(a)-11 clearly purports to restrict the ability of defined benefit plans to distribute a portion of a participant's accrued benefit without complying with specified valuation rules as set forth in

Treasury Regulation § 1.417(e)-1(d).[7] However, the court can find no congressional authorization for the expansion of ERISA § 203(e) effected by Treas.Reg. § 1.411(a)-11. Plaintiff has not directed the court to any authority under which Treas.Reg. § 1.411(a)-11(a) expanded the scope of ERISA § 203(e) or IRC § 411 or any policy reasons why such an expansion should be given effect.

What is produced in the world by the regulations is this: An employer such as the Defendant, chooses to compound the employee's hypothetical balance monthly at a rate in excess of any rate required by law. At early termination the employee has the options, among others, of receiving either the normal annuity at age 65 or the full amount of his hypothetical account. If, as here, his account is large enough, the election is voluntary and the participant is free to make the decision that he thinks is in his economic best interest. He may decide that an annuity at the normal retirement age under the plan may have greater value, or he may believe that he can best the compounding rate used by his employer and take the lump sum. In no way can it be said that the plan unfairly divests him of his due. It is difficult to see how the regulations implement any objective of ERISA.

It may be contended that he is forfeiting some of his normal benefit. There are two answers to that. The first is that he is free to take either. The second is that it is only made to appear that there is a difference in value by a computational contrivance that has only slight connection to economic reality. The parties say that under the regulations the balance in the hypothetical account is run out to age 65 using the more generous rate selected by the employer, and then is discounted back to present value at the Pension Benefit Guaranty Corporation rate, which was said at argument to be about 4.5%. Even today, when interest rates

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[7] The court notes that I.R.S. Notice 96-8, 1996-1 C.B. 359, evidences such an intent on the part of the Treasury Department.

are remarkably low and the yield curve on government bonds is almost flat, this discount rate is about one point lower than would be available to the participant in some of the most conservative of investments. These regulations, then, do not so much preserve benefit value as they create an economic windfall not intended by ERISA.

Accordingly, the court finds the portion of Treas.Reg. § 1.411(a)-11 at issue in this case an unreasonable construction of the congressional mandate set forth in ERISA § 203(e). The interpretation of the Secretary is clearly beyond the scope of the language of the statute, and the court has found no evidence outside the statute to explain the expansion. Instead, the court finds a substantive right, unsupported by the text of ERISA, created by the Secretary of Treasury without authorization from a congressional mandate. Therefore, under *Chevron*, the court cannot find that the interpretation reflected in Treas.Reg. § 1.411(a)-11 meets the minimum threshold of reasonableness needed to give it force and effect.

Because the portion of Treas.Reg. § 1.411-11(a) relied upon by Plaintiff has been deemed by the court to be an unreasonable regulation incorporated under ERISA § 203(e), Plaintiff cannot rely upon the Treasury Regulations as the source of his substantive right in the instant case. Without the application of Treasury Regulations §§ 1.411(a)-11(d) and 417(e)-1(d), Plaintiff has no evident cause of action under ERISA § 203(e). Accordingly, Plaintiff's motion for summary judgment must be denied and Defendants' motion for summary judgment granted.

III. CONCLUSION

Defendants' motion for summary judgment [22-1] is GRANTED and Plaintiff's cross motion for summary judgment [23-1] is DENIED.

SO ORDERED.

APPENDIX C

[Filed Oct. 25, 2000]

IN THE UNITED STATES COURT OF APPEALS
FOR THE ELEVENTH CIRCUIT

No. 99-10640-GG

JERRY L. LYONS, individually and on behalf of all others persons similarly situated,
Plaintiff-Appellant,

versus

GEORGIA PACIFIC CORPORATION SALARIED EMPLOYEES RETIREMENT PLAN, GEORGIA PACIFIC CORPORATION,
Defendants-Appellees.

On Appeal from the United States District Court for the Northern District of Georgia

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ON PETITION(S) FOR REHEARING AND PETITION(S) FOR REHEARING EN BANC

(Opinion _____, 11th Cir., 19___, ___ F.2d ___).

Before: CARNES, BARKETT and WILSON, Circuit Judges.

PER CURIAM:

The petition(s) for Rehearing are DENIED and no member of this panel nor other Judge in regular active service on the Court having requested that the Court be polled on rehearing en banc (Rule 35, Federal Rules of Appellate Procedure; Eleventh Circuit Rule 35-5), the Petition(s) for Rehearing En Banc are DENIED.

ENTERED FOR THE COURT:

/S/ [illegible]
UNITED STATES CIRCUIT JUDGE

APPENDIX D

FEDERAL STATUTE AND REGULATIONS

26 U.S.C. §1053 (1993) Minimum vesting standards

* * * *

(e) Consent for distribution; present value; covered distributions

(1) If the present value of any nonforfeitable benefit with respect to a participant in a plan exceeds $3,500, the plan shall provide that such benefit may not be immediately distributed without the consent of the participant.

"(2)(A) For purposes of paragraph (1), the present value shall be calculated— ,

> "(i) by using an interest rate no greater than the applicable interest rate if the vested accrued benefit (using such rate) is not in excess of $25,000, and
>
> "(ii) by using an interest rate no greater than 120 percent of the applicable interest rate if the vested accrued benefit exceeds $25,000 (as determined under clause (i)).

In no event shall the present value determined under subclause (II) be less than $25,000.

"(B) For purposes of subparagraph (A), the term 'applicable interest rate' means the interest rate which would be used (as of the date of the distribution) by the Pension Benefit Guaranty Corporation for purposes of determining the present value of a lump sum distribution on plan termination."

(3) This subsection shall not apply to any distribution of dividends to which section 404(k) of title 26 applies.

(Pub. L. 93-406, title I, § 203, Sept. 2, 1974, 88 Stat. 854; Pub. L. 96-364, title III, § 303, Sept. 26, 1980, 94 Stat. 1292; Pub. L. 98-397, title I, §§ 102(b), (c), (d)(2), (e)(2), 105(a),

Aug. 23, 1984, 98 Stat. 1426-1428, 1436; Pub. L. 99-514, title XI, §§ 1113(e)(1), (2), (4)(A), 1139(c)(1), title XVIII, § 1898(a)(1)(B), (4)(B)(i), (d)(1)(B), (2)(B), Oct. 22, 1986, 100 Stat. 2447, 2448, 2487, 2942, 2944, 2955; Pub. L. 101-239, title VII, §§ 7861(a)(I), (5)(B), (6)(B), 7862(d)(4), (5), (10), 7891(a)(1), (b)(1), (2), 7894(c)(3), Dec. 19, 1989, 103 Stat. 2430, 2434, 2445, 2449.)

Treasury Regulation § 1.411(a)—11 (1988) Restriction and valuation of distributions.

(a) Scope—(1) In general. Section 411(a)(11) restricts the ability of a plan to distribute any portion of a participant's accrued benefit without the participant's consent. Section 411(a)(11) also restricts the ability of defined benefit plans to distribute any portion of a participant's accrued benefit in optional forms of benefit without complying with specified valuation rules for determining the amount of the distribution. If the consent requirements or the valuation rules of this section are not satisfied, the plan fails to satisfy the requirements of section 411(a).

* * * *

[T.D. 8219, 53 FR 31853, Aug. 22, 1988; 53 FR 48534, Dec. 1, 1988]

Treasury Regulation § 1.417(e)-1 (1993) Restrictions and valuations of distributions from plans subject to sections 401(a)(11) and 417.

* * * *

(d) Present value requirement—(1) Requirements. For purposes of determining the present value of any accrued benefit and for purposes of determining the amount (subject to sections 411(c)(3) and 415) of any distribution including a single sum, a defined benefit plan is subject to the interest rate limitations described in subparagraph (2) of this paragraph (d) at the time set forth in subparagraph (3) of this paragraph (d). A plan amendment that changes the rate

described in this paragraph (d) is subject to section 411(d)(6). The present value of any optional form of benefit can not be less than the present value of the normal retirement benefit determined in accordance with this paragraph.

(2) Section 417 interest rate. The section 417 interest rate is (i) the rate or rates that would used by the Pension Benefit Guaranty Corporation" (PBGC) for a trusteed single-employer plan to value the participant's (or beneficiary's) vested benefit ("applicable interest rate") if the present value of such benefit does not exceed $25,000 (ii) and 120 percent of the applicable interest rate, determined in accordance with (i) above, if such present value exceeds $25,000. In no event shall the present value determined by use of 120 percent of the applicable interest rate result in a present of the less than $25,000. The applicable interest rate may be a series of interest rates for any given date. For example, the applicable rate could be X percent for the first 5 years over which the benefits are valued, Y percent for the next succeeding 10 years and Z percent for the following years. In such case, 1.20 percent of the applicable interest rate would be 1.20 times X percent, 1.20 times Y percent and 1.20 times Z percent over the years described above. The applicable interest rates are the interest rates that would be used (as of the date of the distribution) by the PBGC for purposes of the present value of that benefit upon termination of an insufficient trusteed single-employer plan. Except as otherwise provided by the Commissioner, the applicable interest rates are determined by PBGC regulations. See 29 CFR part 2619 for the applicable PBGC rates.

(3) Time for determining interest rate. (i) Except as provided in subdivision (ii), the section 417 interest rate limitations are determined on either the annuity starting date or the first day of the plan year that contains the annuity starting date. The plan must provide which date is applicable.

(ii) The plan may provide for the use of any other time for determining the interest rate provided that such time is not

more than 120 days before the annuity starting date if such time is determined in a consistent manner and is applied uniformly to all participants.

(iii) The Commissioner may in revenue rulings, notices or other documents of general applicability prescribe other times for determining the section 417 interest rate limitations.

(iv) If a plan amendment changes the time for determining the section 417 interest rate, the amendment will not be treated as reducing an accrued benefit if the conditions of this subdivision (iv) are satisfied. Any distribution in the one-year period commencing at the time the plan amendment is effective (if the amendment is effective on or after the adoption date) must use the rate determined under the plan, either before or after the amendment, that results in the larger accrued benefit. If the plan amendment is adopted retroactively (that is, the amendment is effective prior to the adoption date), the plan must use the rate resulting in the larger accrued benefit for the period beginning with the effective date and ending one year after the adoption date.

(4) Determination of interest rates. (i) In the case of a defined benefit plan that uses a rate or rates in addition to the section 417 interest rate, the rate producing the greatest benefit must be used.

(ii) The same interest rate that is required to be used by the plan under this paragraph (d) to determine the amount of benefit must also be used to compute the present value of the benefit for purposes of determining whether consent for a distribution is required under paragraph (b) of this section.

(iii) Example. A qualified defined benefit plan provides that single sum distributions received on or before normal retirement age are to be determined using the lower of the rate(s) of interest guaranteed under a particular annuity contract of an unrelated insurance company or the applicable section 417 rates. The rates of interest guaranteed under the

annuity contract are 10% for the first 5 years, 7.5% for the next 10 and 5% thereafter while the applicable section 417 interest rates would be 8% and 120% of such rate would be 9.6%. Because in some years over which a benefit is valued the interest rate under the PBGC rates would be the lower rate while in other years it would be the higher rate, the rate that must be used is the one that results in the greater plan benefit.

(5) Exceptions. This paragraph (d) (other than the reference to section 411(d)(6) requirements) does not apply to the amount of a distribution under a nondecreasing annuity payable for a period not less than the life of the participant or, in the case of a QPSA, the life of the surviving spouse. A nondecreasing annuity includes a QJSA, QPSA and an annuity that decreases merely because of the cessation or reduction of Social Security supplements or qualified disability payments (as defined in section 411(a)(9)).

(6) Defined contribution plans. Because the accrued benefit. in a defined contribution plan equals the account balance, such plans are not subject to the interest rate requirements of this paragraph (d), even though they are subject to section 401(a)(11).

* * * *

[T.D. 8219, 53 FR 31854, Aug. 22, 1988; T.D. 8219, 53 FR 48534, Dec. 1, 1988]

APPENDIX E

I.R.S. NOTICE

CASH BALANCE PENSION PLANS

Notice 96-8

I. Purpose

This notice describes and requests comments on proposed guidance concerning the application of sections 411 and 417(e) to single sum distributions under defined benefit pension plans that are cash balance plans. The proposed guidance is being described in this notice in order to permit advance public comment in anticipation of the publication of regulations that incorporate the proposed guidance.

II. Background

A. General description of cash balance plans

In general terms, a cash balance plan is a defined benefit pension plan that defines benefits for each employee by reference to the amount of the employee's hypothetical account balance. An employee's hypothetical account balance is credited with hypothetical allocations and hypothetical earnings determined under a formula selected by the employer and set forth in the plan. These hypothetical allocations and hypothetical earnings are designed to mimic the allocations of actual contributions and actual earnings to an employee's account that would occur under a defined contribution plan. Cash balance plans often specify that hypothetical earnings (referred to in this notice as interest credits) are determined using an interest rate or rate of return under a variable outside index (*e.g.*, the annual yield on one-year Treasury securities). Most cash balance plans also are designed to permit, after termination of employment, a distribution of an employee's entire accrued benefit in the form of a single sum distribution equal to the employee's

hypothetical account balance as of the date of the distribution. Many cash balance plans also provide that if distribution is in the form of an annuity, the amount of the annuity is determined by dividing the hypothetical account balance by an annuity conversion factor.

As explained below, in order to comply with sections 411(a) and 417(e) in calculating the amount of a single sum distribution under a cash balance plan, the balance of the employee's hypothetical account must be projected to normal retirement age and then the employee must be paid at least the present value, determined in accordance with section 417(e), of that projected hypothetical account balance. If a cash balance plan provides interest credits using an interest rate that is higher than the section 417(e) applicable interest rate, payment of a single sum distribution equal to the hypothetical account balance as a complete distribution of the employee's accrued benefit may result either in a violation of section 417(e) or a forfeiture in violation of section 411(a). This is because, in such a case, the present value of the employee's accrued benefit, determined using the section 417(e) applicable interest rate, will generally exceed the hypothetical account balance. The following example illustrates this potential problem.

Example. A cash balance plan provides for interest credits at a fixed rate of 8% per annum that are not conditioned on continued employment, and for annuity conversions using the section 417(e) applicable interest rate and mortality table. A fully vested employee with a hypothetical account balance of $45,000 terminates employment at age 45 and elects an immediate single sum distribution. At the time of the employee's termination, the section 417(e) applicable interest rate is 6.5%.

The projected balance of the employee's hypothetical account as of normal retirement age is $209,743. If $209,743

is discounted to age 45 at 6.5% (the section 417(e) applicable interest rate), the present value equals $59,524.

Accordingly, if the plan paid the hypothetical account balance of $45,000, instead of $59,524, the employee would receive $14,524 less than the amount to which the employee is entitled.

Even if a cash balance plan provides interest credits using an interest rate that exceeds the section 417(e) applicable interest rate, the plan can satisfy sections 417(e) and 411(a). Such a plan would provide that the amount of any single sum distribution is equal to the present value of the employee's accrued benefit determined in a manner that satisfies sections 411(a) and 417(e) even if the amount of the single sum exceeds the employee's hypothetical account balance. Thus, in the example above, the plan would satisfy sections 411(a) and 417(e) if the employee received a single sum distribution of $59,524 (the present value of the employee's accrued benefit) rather than $45,000 (the employee's hypothetical account balance).

B. Existing regulatory safe harbor for cash balance plans

Section 1.401(a)(4)-8(c) of the Income Tax Regulations, as issued in September 1991, provides a safe harbor testing method for cash balance plans. Under this method, a cash balance plan could be tested for nondiscrimination as though it were a defined contribution plan with actual allocations equal to the amount of the hypothetical allocations credited for the plan year. In order to use the safe harbor, a cash balance plan must satisfy certain design requirements that relate to the accrued benefit and valuation rules that are unique to defined benefit plans.

Comments on the September 1991 regulations expressed concern that the safe harbor plan design requirements reflected an interpretation by the Service and Treasury of the qualification requirements that, in certain cases, would

require cash balance plans to pay a single sum distribution in excess of the hypothetical account balance. Guidance was requested on the circumstances in which a cash balance plan (whether or not it qualifies for safe harbor nondiscrimination testing) is permitted to distribute a single sum distribution equal to the hypothetical account balance without violating section 411(a) or 417(e).

When revised regulations under section 401(a)(4) were issued in September 1993, the safe harbor testing method for cash balance plans was left unchanged. The Preamble to those regulations indicated that the safe harbor testing method for cash balance plans had generated significant comment and that further guidance would be issued at a later date.

III. Analysis

A. Nonforfeiture and accrual rules

A cash balance plan is a defined benefit plan, not a defined contribution plan, because the benefits provided are not based solely on actual contributions and forfeitures allocated to an employee's account and the actual investment experience and expenses of the plan allocated to the account. Section 411(a)(7) defines an employee's accrued benefit differently for defined benefit plans than for defined contribution plans. Also, defined benefit plans are subject to a number of statutory provisions that do not apply to defined contribution plans. These include the rules of section 411(b)(1) that limit "backloading" of accruals; the valuation rules of section 417(e); and the definitely determinable benefits requirement of section 401(a)(25). These provisions limit the extent to which a cash balance plan can mimic the benefit and accrual structure of a defined contribution plan.

Under section 411(a)(2), an employee's accrued benefit must become nonforfeitable in accordance with one of the schedules specified in that section. Under § 1.411(a)-7 (a)(1)(ii), the term "accrued benefits" generally refers only to

pension or retirement benefits. Under section 411(b)(1), the accrual of the retirement benefits payable at normal retirement age must satisfy one of the rules in section 411(b)(1)(A), (B) or (C).

Under a cash balance plan, the retirement benefits payable at normal retirement age are determined by reference to the hypothetical account balance as of normal retirement age, including benefits attributable to interest credits to that age. Thus, benefits attributable to interest credits must be taken into account in determining whether the accrual of the retirement benefits under a cash balance plan satisfies one of the rules in section 411(b)(1)(A), (B) or (C). Moreover, benefits attributable to interest credits are in the nature of accrued benefits within the meaning of § 1.411(a)-7(a), rather than ancillary benefits, and thus, once accrued, must become nonforfeitable in accordance with a vesting schedule that satisfies section 411(a).

Cash balance plans can be categorized based on when the benefits attributable to interest credits accrue. Under one type of cash balance plan (referred to in this notice as a frontloaded interest credit plan), future interest credits to an employee's hypothetical account balance are not conditioned upon future service. (Of course, benefits attributable to future interest credits may be forfeited in accordance with the plan's vesting provisions, to the extent permitted under section 411.) Thus, in the case of a frontloaded interest credit plan, the benefits attributable to future interest credits with respect to a hypothetical allocation accrue at the same time that the benefits attributable to the hypothetical allocation accrue. As a result, if an employee terminates employment and defers distribution to a later date, interest credits will continue to be credited to that employee's hypothetical account.

A second type of cash balance plan (referred to in this notice as a backloaded interest credit plan) conditions future interest credits upon further service. In the case of a

backloaded interest credit plan, benefits attributable to interest credits do not accrue until the interest credits are credited to the employee's account. Because backloaded interest credit plans typically will not satisfy any of the accrual rules in section 411(b)(1)(A), (B) or (C), it is anticipated that the proposed guidance will address only frontloaded interest credit plans.

B. Single sum distributions from frontloaded interest credit plans

As indicated above, most cash balance plans are designed to permit a distribution of an employee's entire accrued benefit, after termination of employment, in the form of a single sum equal to the employee's hypothetical account balance as of the date of the distribution. In order for a defined benefit plan to satisfy section 417(e), any single sum distribution payable to an employee from the plan must not be less than the nonforfeitable portion of the present value of the employee's accrued benefit under section 411(a)(7) (determined using the applicable interest rate and mortality table under section 417(e)).

1. Determination of the accrued benefit

In the case of a frontloaded interest credit plan, an employee's accrued benefit as of any date before attainment of normal retirement age is based on the employee's hypothetical account balance as of normal retirement age, including future interest credits to that age. If such a plan specifies a fixed interest rate for use in determining future interest credits, the employee's hypothetical account balance as of normal retirement age (including future interest credits) can be calculated precisely before normal retirement age. However, if a frontloaded interest credit plan specifies a variable outside index for use in determining the amount of interest credits, the precise dollar amount of an employee's hypothetical account balance as of normal retirement age

(including future interest credits to normal retirement age), and thus the precise dollar amount of the employee's accrued benefit as of any date before normal retirement age, cannot be calculated prior to normal retirement age.

A frontloaded interest credit plan that specifies a variable outside index for use in determining the amount of interest credits must prescribe the method for reflecting future interest credits in the calculation of an employee's accrued benefit. In order to comply with section 401(a)(25), the method, including actuarial assumptions, if applicable, must preclude employer discretion. Further, in determining the amount of an employee's accrued benefit, a forfeiture, within the meaning of § 1.411(a)-4T, will result if the value of future interest credits is projected using a rate that understates the value of those credits or if the plan by its terms reduces the interest rate or rate of return used for projecting future interest credits. A forfeiture in violation of section 411(a) also will occur if, in determining the amount of an employee's accrued benefit, future interest credits are not taken into account (*i.e.*, there is no projection of future interest credits) and this has the same effect as using a rate that understates the value of future interest credits.

2. Calculation of the present value of the employee's accrued benefit

In the case of a frontloaded interest credit plan, a single sum distribution optional form of benefit equal to the hypothetical account balance will satisfy section 417(e) only if the single sum distribution is not less than the present value of the employee's accrued benefit calculated in accordance with the applicable interest rate and mortality table under section 417(e)(3). As noted above, the amount of the employee's accrued benefit must be determined using a method of reflecting future interest credits that satisfies section 401(a)(25) and that does not create a forfeiture in violation of section 411(a).

3. Situations in which the present value will not exceed the hypothetical account balance

A frontloaded interest credit plan might provide that the amount of interest credits is determined using a variable interest rate or rate of return that, by its terms, is no greater than the applicable interest rate under section 417(e)(3). For example, a plan that has been amended to comply with the changes to section 417(e) made by the Retirement Protection Act of 1994 (RPA '94) might provide that interest credits are determined using the lesser of the current rate of interest on 30-year Treasury securities or the current yield on 1-year Treasury Constant Maturities. Under such a plan, future interest credits can, without violating section 411(a), be projected to normal retirement age using a rate that is no greater than the applicable interest rate under section 417(e)(3). In that case, assuming that the annuity conversion factor under the plan is not less than the annuity conversion factor determined using the applicable interest rate and mortality table under section 417(e)(3), the employee's hypothetical account balance will equal or exceed the present value of the employee's accrued benefit determined in accordance with section 417(e). Thus, a single sum distribution equal to the employee's hypothetical account balance under such a plan will satisfy sections 411(a) and 417(e).

In other cases, a single sum distribution equal to an employee's hypothetical account balance will satisfy sections 417(e) and 411(a) if (a) the annuity conversion factor is not less than the annuity conversion factor determined using the applicable interest rate and mortality table under section 417(e)(3), (b) under the method for reflecting future interest credits in the calculation of an employee's accrued benefit, the future interest credits are projected using a rate that is no greater that the applicable interest rate under section 17(e)(3),

and (c) this projection does not result in a forfeiture in violation of section 411(a).

By contrast, if the interest rate or rate of return under the plan used in determining the amount of interest credits is high relative to the section 417(e)(3) interest rate, the plan cannot distribute a single sum equal to the employee's hypothetical account balance and satisfy sections 411(a) and 417(e). If such a plan provided that, in determining an employee's accrued benefit, the rate used for projecting the amount of future interest credits was no greater than the interest rate under section 417(e)(3), the projection would result in a forfeiture. Alternatively, if the plan provided for interest credits to be projected using a rate that exceeded the section 417(e) interest rate but then provided for the benefit to be discounted using that same higher rate, the plan would violate section 417(e).

C. Effect of defining the accrued benefit as the hypothetical account balance

The requirements referred to in this notice apply even in the case of a cash balance plan that defines an employee's accrued benefit as ~~an~~ amount equal to the employee's hypothetical account balance. Section 411(a)(7) defines the accrued benefit in terms of benefits payable under the plan at normal retirement age. In a cash balance plan, for an employee who has not attained normal retirement age, whether the employee's retirement benefit payable at normal retirement age under the plan includes benefits attributable to future interest credits depends on whether those benefits have accrued.

If benefits attributable to future interest credits have accrued, and those benefits are disregarded when benefits commence before normal retirement age, the plan has effectively conditioned entitlement to the benefits attributable to those future interest credits on the employee not taking a

distribution prior to normal retirement age. Pursuant to § 1.411(a)-4T, a right that is conditioned under the plan on a subsequent forbearance is a forfeitable right. Accordingly, conditioning entitlement to benefits on the employee not taking a distribution violates the nonforfeitability requirements of section 411(a).

Alternatively, if the benefits attributable to future interest credits have not accrued and will accrue only as of the later dates when the interest credits are included in the hypothetical account balance, the timing of those later accruals must be taken into account in applying the accrual rules of section 411(b)(1). As a result, such a plan typically will not satisfy those accrual rules.

IV. Description of proposal

A. Variable interest rates that may be assumed for these purposes to be no greater than the 30-year Treasury interest rate

It is anticipated that the regulations will set forth a list of standard indices and associated margins for use with frontloaded interest credit plans that provide interest credits equal to the product of the balance of the hypothetical account and the current value of a variable index. (It is anticipated that this proposal will apply without regard to how frequently the rate used to determine interest credits is compounded.) Under a frontloaded interest credit plan that, for this purpose, specifies a variable index equal to the PBGC immediate rate or the sum of one of the standard indices and a margin not greater than the specified margin associated with that standard index, no impermissible forfeiture would result from projecting that the rate used to determine future interest credits for an employee is no greater than the applicable interest rate under section 417(e)(3), as amended by RPA '94. Thus, if such a plan has been amended to comply with the changes to section 417(e) made by RPA '94, the employee's

entire accrued benefit could be distributed in the form of a single sum distribution equal to the employee's hypothetical account balance without violating section 411(a) or 417(e), provided that the plan provides the appropriate annuity conversion factors.

The table below provides the proposed list of standard indices and associated margins. The discount rates on Treasury bills and the yields on Treasury Constant Maturities are the rates reported in the Federal Reserve Bulletin, and the Consumer Price Index is CPI-U, as reported by the Department of Labor. Authority would be delegated to the Commissioner to approve other indices and associated margins.

Standard Index	Associated Margin
The discount rate on 3-month Treasury Bills	175 basis points
The discount rate on 6-month Treasury Bills or 12-month Treasury Bills	150 basis points
The yield on 1-year Treasury Constant Maturities	100 basis points
The yield on 2-year Treasury Constant Maturities or 3-year Treasury Constant Maturities	50 basis points
The yield on 5-year Treasury Constant Maturities or 7-year Treasury Constant Maturities	25 basis points
The yield on 10-year Treasury Constant Maturities or any longer period Treasury Constant Maturities	0 basis points
Annual rate of change of the Consumer Price Index	3 percentage points

In developing these standard indices and associated margins, the Service and Treasury took into account the historical relationship between each of these indices and the rate of interest on 30-year Treasury securities.

Under the proposal, if a frontloaded interest credit plan specified a variable index for use in determining the amount of interest credits that is equal to the sum of a standard index (listed in the table above) and a margin that exceeds the specified margin associated with that standard index, distribution of a single sum equal to the employee's hypothetical account balance would not satisfy both section 411(a) and section 417(e). If such a plan provided that the rate used for projecting the amount of future interest credits was no greater than the interest rate under section 417(e)(3), the projection would result in a forfeiture. Alternatively, if a frontloaded interest credit plan provided for interest credits to be projected using a rate that exceeded the section 417(e) interest rate but then provided for the benefit to be discounted using that same higher rate, the plan would violate section 417(e).

B. Guidance will be prospective

The anticipated regulations will be effective prospectively. In addition, for plan years beginning before the regulations are effective, a frontloaded interest credit plan would not be disqualified for failing to satisfy section 411(a) or 417(e) if the amount of the distribution satisfied those sections based on a reasonable, good-faith interpretation of the applicable provisions of the Code, taking into account pre-existing guidance. For this purpose, plans that comply with the guidance in this notice are deemed to be applying a reasonable, good faith interpretation.

V. Comments

The Service and Treasury invite comments on the proposal described in this notice. Comments are specifically requested on other indices for which guidance may be appropriate and on guidance that would facilitate the transition to use of an approved index (including possible guidance with respect to the application of section 411(d)(6)). Any suggestion of an index (and associated margin, if any) should include an analysis of the historical relationship between the index and the rate for 30-year Treasury securities. Comments should be submitted in writing, referencing Notice 96-7, and addressed to—

Associate Chief Counsel
(Employee Benefits and Exempt Organizations)
CC: EBEO
ATTN: Cash Balance Guidance
Room 5214
Internal Revenue Service
1111 Constitution Ave., N.W.
Washington, D.C. 20224

APPENDIX F

GEORGIA-PACIFIC CORPORATION SALARIED EMPLOYEES RETIREMENT PLAN

AS AMENDED AND RESTATED EFFECTIVE JANUARY 1, 1989

[Sections 1.1, 6.2, 6.3(a), 6.4(a), 8.2]

* * * *

ARTICLE 1

DEFINITIONS

The following words and phrases as used herein shall have the following meanings, unless a different meaning is plainly required by context:

1.1 *Accrued Benefit.* Accrued Benefit means, as of the time of reference, a monthly amount of benefit, payable in the form of an increasing life annuity, commencing on a Participant's Normal retirement Date, where the amount of such monthly benefit is the result of dividing the then credits to such Participant's Personal Account by the applicable factor from Section A of Appendix A.

* * * *

ARTICLE 6

PAYMENT OF BENEFITS

* * * *

6.2 *Standard Benefit.* The normal form of benefit payable to a Participant who is not married at his Benefit Commencement Date is an increasing annuity for the life of the Participant . . . .

* * * *

6.3 *Standard Benefit for Married participants.*

(a) The normal form of benefit payable to a Participant who is married at his Benefit Commencement Date is a joint and fifty percent (50%) surviving spouse increasing annuity . . . .

* * * *

6.4 *Optional Forms of Benefit.*

(a) An unmarried Participant, or a married Participant who has made an election under Section 6.3(e), May elect to receive, in lieu of the standard form of benefit in Sections 6.2 of 6.3, a benefit in one of the optional forms described below:

* * * *

Option C: Lump Sum Payment. A single Lump sum payment equal to the amount credited to the Participant's Personal Account as of the end of the month preceding his Benefit Commencement Date.

* * * *

ARTICLE 8

ADMINISTRATION OF THE PLAN

* * * *

8.2 *Powers and Duties.* The Plan Administrator shall have complete discretionary control of the administration of this Plan, with all powers necessary to enable it properly to carry out its duties in that respect, including the power to construe this plan and to resolve all equitable and other questions that arise under this Plan. All disbursements by the Trustee shall be made upon, and in accordance with, the written instructions of the Plan Administrator. The decisions

of the administrator on all matters within the scope of its authority shall be final and binding upon all affected parties, including Participants and Beneficiaries.

APPENDIX G

IRS FORM 5624 (Rev. 5-91)

Employee Benefit Plan
Defined Benefit Plans Minimum Vesting Standards
(Worksheet Number 2A – Determination of Qualification)
[2000]

INSTRUCTIONS—All items must be completed. A "Yes" answer generally indicates a favorable conclusion is warranted while a "No" answer indicates a problem exists. Please use the space on the worksheet to explain any "No" answer. See Document 6390, Explanation Number 2A, for guidance in completing this form.

(The technical principles in this worksheet may be changed by future regulations or guidelines.)

[Items V & VII]

* * * *

V. Cash-Outs and Immediate Distributions [2031]

a. For purposes of determining an employee's accrued benefit that resulted from employer contributions, does the plan not disregard years of service performed for which the employee received a cash-out? [2032]

(If the answer is "Yes," skip to (f).)

b. If an involuntary cash-out, must the employee receive a distribution of the present value of the entire non-forfeitable benefit that resulted from employer contributions? [2033]

c. Are such distributions made because of the termination of the employee's participation in the plan? [2034]

d. Is the value of the employee's accrued benefit restored when the employee repays the full amount of the distribution as provided by regulations? [2035]

e. Does the plan disregard service only for which an employee receives payment? [2036]

f. Is the interest rate for valuing accrued benefits and determining the amount of distribution specified by the plan? [2037, 2038]

g. Does the plan satisfy the section 417 interest rate limitations as amended by section 1139 of TRA '86? [2037, 2038]

h. Does the plan determining the section 417 interest rate limitation as of the date of distribution or the first day of the plan year? [2039]

i. If the plan uses an interest rate in addition to the section 417 rate, does it provide that the present value of vested accrued benefits and the amount of distributions will be determined using the rate which results in the greatest benefit? [2040]

j. Are immediate distributions, where the present value of the vested accrued benefit has ever exceeded $3,500, precluded unless the participant consents? [2041]

* * * *

VII. Accrued Benefits [2045]

a. Insured Plans [2046]

i. Is the plan funded exclusively with insurance contracts satisfying the requirements of Code section 412(i)? *(If the answer is "Yes," complete only questions b(i) and f of this worksheet.)* [2047]

b. General [2048]

i. Does the plan provide neither a decrease in benefit payments to a participant (*or beneficiary*), not a decrease in a separated participant's rights to benefits, because of an increase in social security benefits? [2049]

ii. Does the plan provide for an accrual computation period for purposes of providing an accrued benefit? [2050]

iii. For purposes of benefit accrual, does the plan take into account every year required by DOL Regulations? [2051]

iv. If an employee may begin participation on a date other than the first day of an accrual computation period, does the plan provide for a partial year of participation as required by the DOL Regulations? [2052]

v. Does the plan not defer the accrual of benefits on behalf of an employee beyond the completion of 2 continuous years of service? [2053]

vi. If the plan defers accruals during a period of up to a participant's first 2 years of service, does the participant retroactivity accrue a benefit for that period after it ends? [2053]

c. Normal Retirement Benefit [2056]

i. Is the plan's accrued benefit always ascertainable? [2057]

ii. Is the plan's normal retirement benefit, as specified in the plan, equal to the plan's greatest early retirement benefit, or the benefit at normal retirement age, whichever is greater? [2058]

d. Methods [2060]

Once a plan satisfies the requirements of either i, ii, or iii, DO NOT complete the remaining items of section d.

i. 133-1/3 Percent Test

A. Is the accrued benefit that becomes payable at normal retirement age equal to the plan's normal retirement benefit? [2062]

B. Is the accrual rate in any given year under the plan no greater than 133-1/3 percent of the accrual rate in any prior year (*make appropriate adjustments for ancillary benefits*)? [2062]

If the answer is "Yes", DO NOT complete the remainder of section d.

ii. 3 Percent Test *(Use this test last for Unit Benefit Plans).*

A. In a fully integrated excess or offset plan, does the plan prohibit an early retirement benefit? *(If the answer is "No," use another test.)* [2062]

B. If the plan bases its benefits on average compensation, does it specify that the benefit is determined on the basis of compensation averaged over consecutive years of service, not more than 10, which yield the highest average? *(If the answer is "No," the 3 percent test cannot be met.)* [2062]

C. Is the accrual of plan benefits based on a "normal retirement benefit" which is figured assuming the earliest possible entry age under the plan? *(If no entry age is specified by the plan, use a 0.)* [2062]

D. If a participant does not accrue the "normal retirement benefit" by normal retirement age, are years of participation after normal retirement age

counted for purposes of meeting the requirement that the benefit accrued at the rate of at least 3 percent a year? [2062]

E. Does the plan specify the accrual of the "normal retirement benefit" will be a rate of at least 3 percent of the benefit each year of participation? [2062]

Check "Yes" if the 3 percent Test is satisfied. *(If all answers above are "Yes," this test is satisfied.)* If this test if satisfied, do not complete remainder of this section.

If the answer to B., C., and D. is "Yes," but the answer to E. if "No," then complete F.

F. Can it be demonstrated mathematically that the plan's "normal retirement benefit" accrues at a rate of at least 3 percent for each year of participation? In making this calculation, assume the earliest possible entry age under the plan. *(If no entry age is specified, assume 0.)* See the explanation for guidance in making your mathematical computations. [2062]

iii. Fractional Rule

A. If the plan benefit is based on average compensation, is the average based on compensation for a period no greater than the 10 years if service immediately before the date the benefit is determined? [2062]

B. Does the plan's benefit accrue at the same rate for all years? [2062]

If the answers to A. and B. are "Yes," this rule is satisfied.

C. Is it clear from the language of the plan that if a participant terminates service in year Y that the accrued benefit at Y is at least equal to the product of the plan's normal retirement benefit times a fraction of the actual years of participation from entry to Y over the years of service from entry to normal retirement age? [2062]

e. Coordinating Accrual Rules with Topheavy Rules

Do the accrual benefit rules properly coordinate with the topheavy rules? [2078]

f. Allocation of Accrued Benefits Between Employer and Employee Contributions

If the plan does not provide for employee contributions, DO NOT complete this section. [2080]

i. Does the plan maintain separate accounts for voluntary employee contributions? *(IF NO VOLUNTARY CONTRIBUTIONS ARE PERMITTED, CHECK "N/A")* [2081]

ii. Does the plan define the accrued benefit that is the result of employer contributions as the total accrued benefit less the accrued benefit that is the result of mandatory employee contributions? [2082]

iii. If the plan provides for mandatory employee contributions, does it correctly determine the accrued benefit that resulted from these contributions? [2083]

iv. is the interest credited to mandatory contributions calculated in accordance with section 411(c)(2)(C)? [2084]

APPENDIX H

GEORGIA-PACIFIC CORPORATION

LAW DEPARTMENT

DANIEL R. KOPTI,
Senior Counsel

133 Peachtree Street, N.E.
P.O. Box 105605
Atlanta, Georgia 30348-5605
Telephone (404) 652-7388
Facsimile (404) 584-1461

April 17, 1996

SENT VIA OVERNIGHT DELIVERY

Mr. Paul Holzman
National Center for Retirement Benefits, Inc.
666 Dundee Road, Suite 1200
Northbrook, IL 60062

Re: Mr. Jerry Lyons

Dear Mr. Holzman:

Your letter of March 18 to Ms. Becky Crockford has been referred to us for response.

We understand that Mr. Jerry Lyons is concerned about the interest rate used in calculating the lump sum distribution that he received in January 1993 from the Georgia-Pacific Corporation Salaried Employees Retirement Plan ("SERP"). He states in your letter that the Plan Administrator for the SERP must calculate the present value of normal retirement benefits by using an interest rate permitted unders Code Section 417(e) and IRS regulation 1.417(e)-1. He asserts that an incorrect interest rate was used in his case, causing a

reduction in his lump sum distribution. Your letter asks to have his SERP benefits recalculated and to have any additional amounts paid to him, along with interest.

Please be advised that the SERP is a special form of defined benefit plan known as a "cash balance" plan. As described in IRS Notice 96-8, a "cash balance" plan defines benefits for each employee by reference to the amount of the employee's hypothetical account balance. An employee's hypothetical account balance is credited with hypothetical allocations and hypothetical earnings determined under a formula selected by the employer and set forth in the plan. These hypothetical allocations and hypothetical earnings are designed to mimic the allocations of actual contributions and actual earnings to an employee's account that would occur under a defined contribution plan. Most cash balance plans are designed to permit, after termination of employment, a distribution of an employee's entire accrued benefit in the form of a single sum distribution equal to the employee's hypothetical account balance as of the date of the distribution.

According to the Plan Administrator's records, Mr. Lyons terminated employment in January 1991. He elected at that time to postpone receipt of his SERP benefits until a future date. During 1991 and 1992, his personal account was credited with hypothetical earnings (which the SERP calls "credit adjustments") equal to the average Pension Benefit Guaranty Corporation immediate annuity rate in effect for the previous calander year, plus 0.75%. The credit adjustment for 1991 was equal to 8.23%, while the credit adjustment for 1992 was equal to 7.71%, compounded monthly. In November 1992, Mr. Lyons requested a lump sum distribution of his personal account in the SERP. The

distribution took place in January 1993 and was equal to the hypothetical balance in his personal account of $36,109.15. Contrary to Mr. Lyon's assertion, his lump sum distribution was not calculated with reference to the present value of a normal retirement benefit or by using an interest rate that violated IRS requirements.

During the past several months we have exchanged several letters on the issue of whether Mr. Lyons qualifies as a "participant" in the SERP. As stated previously, the Supreme Court concluded in *Firestone Tire and Rubber Co. v. Bruch*, 489 U.S. 101, 117 (1989) that former employees who have no reasonable expectation of returning to covered employment can qualify as "participants" in an employee benefit plan only if they have a colorable claim to vested benefits. We are not persuaded that Mr. Lyons' claim for SERP benefits, as expressed in your letter of March 18, constitutes a colorable claim to vested benefits. However, in the interest of alleviating Mr. Lyons' concerns and as an expression of good faith in this matter, the Plan Administrator for the SERP has decided to provide you with the summary plan description for the SERP. Also, if you would like a copy of the plan document, please send us a check in the amount of $28.75 to pay for photocopying charges (at the rate of 25 cents per page), and the document will be sent to you. The check should be made payable to "Georgia-Pacific Corporation Salaried Employees Retirement Plan". The furnishing of these documents does not constitute an admission by the Plan Administrator that Mr. Lyons is a "participant" in the SERP.

If you have any additional questions or comments regarding this matter, we request that you direct them to our attention.

Very truly yours,

/s/ Daniel R. Kopti
DANIEL R. KOPTI
Senior Counsel

Enclosure
93314

APPENDIX I

May 12, 1989

DEPARTMENT OF THE TREASURY
INTERNAL REVENUE SERVICE
P.O. Box 941
Atlanta, Georgia 30370-000

GEORGIA-PACIFIC CORPORATION
133 PEACHTREE ST NE (BENEFITS-14)
ATLANTA, GA. 30303

District Office Code and Case Serial Number:
53809010

Name of Plan:
GEORGIA-PACIFIC CORPORATION SALARIED EMPLOYEES RETIREMENT PLAN

Application Form:
5300

Employer Identification Number:
930432081

Plan Number:
046

File Number:
580011644

Dear Applicant:

Based on the information supplied, we have made a favorable determination on your application identified above. Please keep this letter in your permanent records.

Continued qualification of the plan will depend on its effect in operation under its present form. (See section 1.401-1(b)(3) of the Income Tax Regulations.) The status of the plan in operation will be reviewed periodically.

The enclosed document describes the impact of Notice 86-13 and some events that could occur after you receive this letter that would automatically nullify it without specific notice from us. The document also explains how operation of the plan may affect a favorable determination letter, and contains information about filing requirements.

This letter relates only to the status of your plan under the Internal Revenue Code. It is not a determination regarding the effect of other Federal or local statutes.

All correspondence should be sent to the address shown above.

The enclosed Caveat Listing(s) should be considered a part of this determination letter.

If you have any questions, please contact EVELYN WAUGH at (404) 331-6971.

Sincerely,

/s/ Paul Williams
PAUL WILLIAMS
District Director

Enclosures:
Caveat Listing(s)
Publication 794
PWBA 515

CAVEAT LISTING FOR: GEORGIA-PACIFIC CORPORATION SALARIED EMPLOYEES RETIREMENT PLAN

PLAN NUMBER: 46

EMPLOYER IDENTIFICATION NUMBER: 930432031

This determination is subject to your adoption of the proposed amendments submitted in your or your representative's letter(s) dated 10/17/83.

The proposed amendments should be adopted on or before the date prescribed by the regulations under Code section 401(b). A copy of the executed amendments should be maintained in your file; however, it is not necessary to forward a copy to this office.

INTERNAL REVENUE SERVICE
DISTRICT DIRECTOR
P.O. BOX 2508
CINCINNATI, OH 45201

Date: May 05 1997

GEORGIA-PACIFIC CORPORATION
C/O LARA B. ROBINSON
C/O KING & SPALDING
191 PEACHTREE STREET
ATLANTA, GA 30303-1763

Employer Identification Number:
93-0432081

DLN:
585250004

Person to Contact:
Cindy Perry

Contact Telephone Number:
(513) 684-3957

Plan Name:
GEORGIA-PACIFIC CORPORATION
SALARIED EMPLOYEES RETIREMENT PLAN

Plan Number:
046

Dear Applicant:

We have made a favorable determination on your plan, identified above, based on the information supplied. Please keep this letter in your permanent records.

Continued qualification of the plan under its present form will depend on its effect in operation. (See section 1.401-1(b)(3) of the Income Tax Regulations.) We will review the status of the plan in operation periodically.

The enclosed document explains the significance of this favorable determination letter, points out some events that may affect the qualified status of your employee retirement plan, and provides information on the reporting requirements for your plan. It also describes some events that automatically nullify it. It is very important that you read the publication.

This letter relates only to the status of your plan under the Internal Revenue Code. It is not a determination regarding the effect of other federal or local statutes.

This determination is subject to your adoption of the proposed amendments submitted in your letter dated July 31, 1996. The proposed amendments should be adopted on or before the date prescribed by the regulations under Code section 401(b).

This determination letter is applicable for the amendment(s) adopted on December 30, 1994.

This determination letter does not apply to the merger, consolidation, or transfer of assets or liabilities of a plan described in Code section 6058(a) to, or with, another plan. A determination has not been made on whether the transaction met the requirements of the income tax regulations under Code section 414(1).

This plan satisfies the minimum coverage requirements on the basis of the average benefit test in section 410(b)(2) of the Code.

This plan satisfies the nondiscrimination in amount requirement of section 401(a)(4)-1(b)(2) of the regulations on the basis of a general test describe to the regulations.

GEORGIA-PACIFIC CORPORATION

This letter is issued under Rev. Proc. 93-39 and considers the amendments required by the Tax Reform Act of 1986 except as otherwise specified in this letter.

This plan satisfies the nondiscriminatory current availability requirements of section 1.401(a)(4)-4(b) of the regulations with respect to those benefits, rights, and features that are currently available to all employees in the plan's coverage group. For this purpose, the plan's coverage group consists of those employees treated as currently benefiting for purposes of demonstrating that the plan satisfies the minimum coverage requirements of section 410(b) of the Code.

This plan also satisfies the requirements of section 1.401(a)(4)-4(b) of the regulations with respect to the specific benefits, rights, or features for which you have provided information.

Except as otherwise specified this letter may not be relied upon with respect to whether the plan satisfies the qualification requirements as amended by the Uruguay Round Agreements Act, Pub. L. 103-465 and by the Small Business Job Protection Act of 1996 (SBJPA), Pub. L. 104-108, other than the requirements of Code section 401(a)(26).

We have sent a copy of this letter to your representative as indicated in the power of attorney.

If you have questions concerning this matter, please contact the person whose name and telephone number are shown above.

Eclosures:
Publication 794
Reporting & Disclosure Guide
for Employee Benefit Plans

Sincerely yours,
/s/ Paul M. Harrington
District Director

Supreme Court, U.S.
FILED
MAR 2 2001
OFFICE OF THE CLERK

No. 00-1234

In The

Supreme Court of the United States

Georgia-Pacific Corporation Salaried Employees Retirement Plan and Georgia-Pacific Corporation,

Petitioners

v.

Jerry L. Lyons, Individually and on Behalf of All Others Similarly Situated,

Respondents.

On Petition for Writ of Certiorari to the United States Court of Appeals for the Eleventh Circuit

Brief in Opposition to Petition for Writ of Certiorari

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March 2, 2001 * Counsel of Record

WILSON-EPES PRINTING CO., INC. – (202) 789-0096 – WASHINGTON, D. C. 20001

QUESTIONS PRESENTED

In the 1950s, Congress sought to encourage employers to provide pension plans for their employees. Accordingly, in 1954, Congress enacted legislation under the Internal Revenue Code ("Code") that (1) enables employers to immediately deduct contributions made to a pension trust established for the purpose of providing pension benefits to the employer's employees, (2) exempts the earnings on the assets in such trusts from taxation, and (3) defers the tax on employees' pension benefits until the pension benefits are actually distributed. *See* 26 U.S.C. §§402(a), 404(a) and 501(a) (A-18, 25). Employers may avail themselves of these tax advantages only if the pension plan is "tax qualified," that is, satisfies the requirements of §401(a) of the Code in *form* and *operation*. 26 U.S.C. §401(a) (A-17).

In the early 1970s, Congress conducted a study on employer-provided pension plans, and found that " many employees with long years of employment [were] losing anticipated retirement benefits" due to the lack of minimum vesting and funding standards. 29 U.S.C. §1001 ("Congressional findings and declaration of policy") (A-1). To remedy this problem, Congress enacted, in 1974, the Employee Retirement Income Security Act ("ERISA"), 29 U.S.C. §1001, *et seq*. Among other things, ERISA establishes minimum vesting and funding standards. 29 U.S.C. §1001 (A-1, 2). Because pension plans are largely tax driven, these same vesting and funding standards are reiterated in the Code.

ERISA and the Code recognize and treat all pension plans as falling into just one of two broad categories: (1) defined benefit; and (2) defined contribution. Petitioners acknowledge that the Georgia-Pacific Corporation Salaried Employees Retirement Plan ("the Plan") is a defined benefit plan. Petition at 5. This case concerns petitioners' computation of the lump sum present value of respondents' accrued benefits, and petitioners' desire to except the Plan from the statutes and regulations governing all defined benefit plans.

Since 1984, ERISA §§203(e) and 205(g),and their Code analogues, Code §§411(a)(11) and 417(e), have regulated the maximum interest rate that may be utilized to compute the lump sum present value of a participant's accrued benefit (here, an annuity commencing at age 65). These statutes eliminate the discretion once exercised by pension plans in selecting the present value discount rate and, thereby, prevent the erosion of the value of the accrued benefit by application of an unreasonably high discount rate. Treasury Regulations ("TRs") 1.411(a)-11(d) and 1.417(e)-1(d), issued in 1988, explain that the calculation for determining the lump sum present value must be performed by reference to the participant's normal retirement benefit (here, the annuity commencing at age 65).

The Eleventh Circuit Court of Appeals held that TRs 1.411(a)-11(d) and 1.417(e)-1(d) reasonably construed ERISA §203(e), and found that petitioners violated ERISA §203(e) by paying Mr. Lyons and the other Class members lump sum benefits that were significantly less than required under the TRs. Four questions are presented:

1. Whether the Plan was required to comply with ERISA §203(e) and TRs 1.411(a)-11(d) and 1.417(e)-1(d)?

2. Whether the Eleventh Circuit Court of Appeals properly conducted a *de novo* review of petitioners' denial of Mr. Lyons' claim where--

    a. Petitioners themselves asserted that the standard of review for "all" issues was *de novo*.

    b. *Firestone Tire & Rubber Co. v. Bruch*, 489 U.S. 101 (1989), cited by petitioners, expressly declined to state the standard of review for claims brought under ERISA remedial provisions other than ERISA §502(a)(1)(B), 29 U.S.C. §1132(a)(1)(B);

c. Mr. Lyons brought his ERISA claim under ERISA §502(a)(3), 29 U.S.C. §1132(a)(3); and

d. Although not required to do so, the Eleventh Circuit Court of Appeals considered petitioners' characterization of Mr. Lyons' accrued benefit and found that it conflicted with unambiguous Plan language defining his accrued benefit?

3. Whether the Eleventh Circuit Court of Appeals correctly held that two IRS determination letters proffered by petitioners and a "safe harbor" in IRS Notice 96-8 related solely to tax qualification where--

a. The determination letters and "safe harbor" in Notice 96-8 expressly state that they address tax qualification, only;

b. The determination letters further state that they are a determination of the Plan's tax status under the Code, and not a determination of the effect of other federal laws;

c. The determination letters do not address any disputed issue;

d. TR 601.201 limits the sections of the Code that may be addressed in a determination letter to §§401, 403(a), 405, and 501(a); and

e. 26 U.S.C. §6110(k)(3) states that IRS determination letters "may not be used or cited as precedent"?

4. Whether petitioners had notice of their obligations under ERISA §203(e) *long before* Mr. Lyons and the other Class members received their improperly

reduced lump sum pension benefits?

PARTIES TO THE PROCEEDINGS

All parties to the proceeding are identified in the caption of the case. Based on the corporate disclosure in the Petition, Georgia-Pacific does not have a parent company, and two publicly traded funds–Longleaf Partners Fund and The Income Fund of America, Inc.–own a beneficial interest of more the 10% of a class of Georgia-Pacific tracking stock (The Timber Group Company (NYSE: TGP)).

A plaintiff class was certified in the United States District Court for the Northern District of Georgia, defined as follows:

> All participants (or beneficiaries of participants) in the Georgia-Pacific Salaried Employees Retirement Plan (the "Plan") (i) who received a lump sum distribution of benefits calculated at a time when such participants had a vested interest in the Plan who (ii) received a distribution of benefits in a lump sum where (iii) at the date as of which the amount of the lump sum was calculated, the lump sum was lower than the present value, if determined using the "applicable interest rate" as defined in Internal Revenue Code Section 417(e)(3) and set forth in Treasury Regulations issued pursuant to Internal Revenue Code Section 417(e), of such participants' accrued benefit, as defined under ERISA.

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OPINIONS BELOW

The relevant opinions below have been attached to the Petition.

JURISDICTION

Mr. Lyons concurs with petitioners' jurisdictional statement.

PRINCIPAL STATUTES AND REGULATIONS INVOLVED

Mr. Lyons concurs with petitioners' statement of the principal statutes and regulations involved.

INTRODUCTION

This case raises no new or novel question of federal law, concerns no split between the federal Courts of Appeals or any state court, and presents no compelling reason for this Court to grant certiorari. Rather, this case involves a straightforward breach by petitioners of ERISA §203(e) and TRs 1.411(a)-11(d) and 1.417(e)-1(d), authority that existed *long* before Mr. Lyons and the other Class members received their improperly reduced lump sum pension benefits. Moreover, the Treasury Department ("Treasury") and Internal Revenue Service ("IRS") have repeatedly rejected the reasoning advanced by petitioners for exempting their type of defined benefit plan from the statutes and regulations governing all other defined benefit plans.

ERISA §§203(e) and 205(g), and their Code analogues, Code §§411(a)(11) and 417(e), require that the lump sum present value of a participant's accrued benefit (here, an annuity commencing at age 65) be *no less than* the present value of such accrued benefit determined utilizing the interest rate set forth in these statutes. *See* 29 U.S.C. §§1053(e) and 1055(g) (A-5, 6); and 26 U.S.C. §§411(a)(11) and 417(e) (A-20-

23). Congress specified a maximum rate in these statutes for computing present value because many employers utilized unreasonably high rates, thereby causing participants's lump sum benefits to be significantly understated. Relevant legislative history during the past sixteen years consistently reaffirms Congress' unequivocal intent to regulate the interest rates utilized to compute the present value of an accrued pension benefit.

Under ERISA §3002(c), Congress authorized the Secretary of the Treasury to promulgate regulations enforcing ERISA §203(e). 29 U.S.C. §1202(c) (A-15). The Treasury did so in 1988 by promulgating TRs 1.411(a)-11(d) and 1.417(e)-1(d), which reiterate the requirements of the statute. 26 C.F.R. §§1.411(a)-11(d) and 1.417(e)-1(d) (A-33, 35, 36). Petitioners ignored ERISA §203(e)'s present value rules and, in computing Mr. Lyons' lump sum benefit, admitted that they did not even attempt to comply with the statute. *See* Letter from Georgia-Pacific to Paul Holzman (A-134). That decision cost Mr. Lyons over 36% of his pension benefits. If anyone has been "whipsawed" and "jerked" (petitioners' characterization of the present value rule), it is Mr. Lyons and the other members of the Class.

Petitioners ask this Court to override Congressional intent and, further, to abandon the Court's traditional deference to long-existing regulations promulgated by the agency charged with enforcing the statute. Specifically, petitioners request that this Court excuse defined benefit plans of the cash balance variety from the present value rules under ERISA §203(e) and TRs 1.411(a)-11(d) and 1.417(e)-1(d). The statute and TRs, however, existed *long before* Georgia-Pacific adopted its cash balance plan, and for an even longer period of time before Mr. Lyons and the other Class members received their improperly reduced lump sum benefits. Further, nowhere do ERISA, the Code or the TRs except *any* type of *defined benefit* plan from the statutory present value rules. Accordingly, there exists no legal or equitable basis for excusing cash balance *defined benefit* plans from the interest rate requirements of ERISA §203(e) or TRs 1.411 and 1.417(e).

Despite the pre-existence of ERISA §203(e) and TRs 1.411(a)-11(d) and 1.417(e)-1(d), and routine *unquestioned* compliance with the statute and TRs by *thousands* of pension plans across the country, petitioners assert that hundreds of cash balance plans will be exposed to "unanticipated liability" if they are not excepted from the present value rules. This hyperbole entirely misrepresents the import of the relevant issues. To date, only one other cash balance plan has been found to have violated ERISA §203(e). In that case, the Second Circuit Court of Appeals unanimously held that the cash balance plan was required to comply with ERISA §203(e) and TRs 1.411 and 1.417(e). *See Esden v. Bank of Boston*, 229 F. 3d 154 (2nd Cir. 2000). Petitioners' error stems from a misunderstanding and misapplication of ERISA's present value rules, not from some inherent inequity or flaw in ERISA's design. Cash balance plans avoid the error committed by petitioners through proper plan design and adherence to the long-standing TRs ignored by petitioners. Indeed, the issues raised by petitioners are, for all intents and purposes, devoid of substance or merit.

Petitioners suggest that the Eleventh Circuit Court of Appeals invented the projection forward, discount back, methodology petitioners were required to use in computing Mr. Lyons' and the other Class members' lump sum benefits. The unambiguous terms of the Plan, however, require interest credits to be projected to normal retirement age (here, age 65) to determine the participant's accrued benefit under the Plan, an annuity commencing at age 65. As the Plan, itself, states that it intends to comply with ERISA and the Code, and applicable regulations, petitioners should have computed the present value of respondents' accrued benefits in accordance with the statutory interest rate, and paid respondents the resultant lump sum.

Petitioners' reliance on two IRS determination letters proffered below is entirely misplaced. All United States Courts of Appeals' opinions hold that an IRS determination letter that does not address the disputed issue(s) is entitled to *no* weight. The determination letters here did not address any

disputed issue. Moreover, they expressly stated that they related solely to the tax status of the Plan under the Code, and were not a determination regarding the effect of other Federal statutes. Thus, the IRS determination letters did not, as petitioners insist, "verify" that the Plan complied with ERISA §203(e).[1]

Petitioners erroneously assert that application of IRS Notice 96-8 to lump sum distributions before January 18, 1996 (the date the Notice was issued) violates the fair notice doctrine. IRS Notice 96-8 is almost exclusively a review of *long-existing* valuation rules applicable to defined benefit plans, in particular, the present value rule under Code §417(e), and the anti-forfeiture rules under Code §411(a) and TR 1.411. The Eleventh Circuit conducted an exhaustive *Chevron*[2] analysis in determining that TRs 1.411(a)-11(d) and 1.417(e)-1(d) represented a reasonable construction of ERISA §203(e). Accordingly, the respect the Eleventh Circuit accorded Notice 96-8 was entirely proper and in no way violated the fair notice doctrine.

Lastly, petitioners improperly raise an issue not raised below. Specifically, petitioners argue that the Eleventh Circuit should have applied a deferential standard of review to petitioners' determination that Mr. Lyons received all he was entitled to receive under ERISA §203(e). However, in their appeal brief below, petitioners agreed with Mr. Lyons that the standard of review with respect to "all" issues was *de novo*. Appellees' Brief at 14. Furthermore, although it was not required to do so, the Eleventh Circuit considered petitioners' interpretation of the Plan and ruled that it conflicted with unambiguous Plan language defining Mr. Lyons' accrued benefit.

---

[1] On appeal below, the Justice Department submitted an amicus brief in support of Mr. Lyons' position in this dispute. The Justice Department acknowledged, therein, that the IRS may have made a mistake in issuing the favorable determination letters.

[2] *Chevron v. Natural Resources Defense Council*, 467 U.S. 837 (1984).

In light of the foregoing, there plainly exists no reason for granting certiorari in this case, much less a "compelling" one. Therefore, Mr. Lyons respectfully requests that this honorable Court deny the Petition.

STATEMENT OF THE CASE

Overview of Cash Balance Defined Benefit Plans

ERISA recognizes just two categories of pension plans: (1) "defined benefit" plans; and (2) "individual account" or "defined contribution" plans. A defined benefit plan is any pension plan that is not a defined contribution plan. 29 U.S.C. §1002(35) (A-4). A defined contribution plan provides an individual account for each participant and determines benefits based solely upon amounts contributed to the account, investment performance of the assets in the account, and forfeitures of accounts of other participants that may be allocated to the account. 29 U.S.C. §1002(34) (A-3).

A defined benefit plan is a pension plan that is not a defined contribution plan, does not create individual accounts for participants, and does not provide benefits based upon investment performance or forfeitures of other participants' accounts. Rather, benefits are based on a formula articulated in the plan, and are paid from plan assets pooled in a common trust fund. *See* 29 U.S.C. §§1081(a) and1082 (a), (b) (A-13,14).

ERISA requires all defined benefit plans to pay participants a benefit in the form of a qualified joint and survivor annuity ("QJSA")--an annuity payable for the life of the participant and, thereafter, for the life of the participant's surviving spouse (if any). 29 U.S.C. §§1055(a)-(e) (A-6). The only exception to this requirement is where the participant and participant's spouse (if any) elect to waive the QJSA, or the present value of the benefit is less than $5,000 [formerly, $3,500]. *Id.* If a lump sum is elected, ERISA §§203(e) and 205(g) direct that the amount distributed be no less than the present value of the annuity benefit, determined in accordance with the interest rate restrictions set forth in these statutes. 29

U.S.C. §§1053(e) and 1055(g) (A-5, 6, 10,11).

Cash balance plans establish *bookkeeping* accounts for participants, which are periodically credited with (1) a percentage of the participant's pay; and (2) interest at a specified rate. IRS Notice 96-8 (A-47, 48); General Accounting Office Report No. GAO/HEHS-00-185 (Sept. 29, 2000) ("GAO Rept.") at 7 (A-109). These accounts are purely hypothetical because a cash balance plan *is* a *defined benefit* plan and, therefore, there can be no individual accounts or contributions to individual accounts. 29 U.S.C. §§1002(34), 1002(35) (A-3, 4); IRS Notice 96-8 (A-47, 48); GAO Rept. at 7, 37-38 (A-109, 118).

Most cash balance plans permit employees to *elect* to receive their annuity benefit in an optional lump sum form, often in an amount equal to the participant's hypothetical account balance. Notice 96-8 (A-48). With rare exceptions, this methodology for determining and paying a lump sum invites no ERISA violations. If the plan's interest crediting rate is no greater than the applicable discount rate, the hypothetical account balance will at least equal the minimum present value required under ERISA §§203(e) and 205(g). *Id.* An ERISA violation arises, however, if the plan's interest crediting rate exceeds the applicable discount rate, as the account balance will be less than the minimum present value and, therefore, payment of an amount equal to the account balance will not satisfy ERISA §203(e). *Id.*

Given the requisite features of defined benefit plans, petitioners are clearly mistaken when they suggest that, in cash balance *defined benefit* plans, (1) the employer contributes to individual accounts; (2) the basic benefit is a single sum; and (3) the present value of the participant's accrued benefit is the account balance. Petition at 5.

Although the advantages (or lack thereof) of cash balance *defined benefit* plans over other type of defined benefit plans were not at issue below, petitioners belatedly argue in their Petition that employers adopt cash balance plans for purely altruistic reasons, and that cash balance plans represent a pension panacea for employees. Petition at 5. However, a recent report concerning cash balance plans, prepared by

economists at the GAO vigorously challenges these conclusions.[3]

The GAO Rept. explains that many employers who convert their traditional defined benefit plans to cash balance plans do so to save costs, often by eliminating early retirement subsidies previously available. GAO Rept. at 12-13 (A-111). Although benefits accrue more rapidly during an employee's early years of service under a cash balance plan than under a "traditional" defined benefit plan (where the reverse is true), many short-service employees who presumably would benefit from the rapid early accruals will not, in fact, receive this benefit. This result occurs because the median tenure of workers age 25 and older is 4.7 years, and most cash balance plans have five-year "cliff" vesting, meaning the employee is unvested in any part of his/her accrued benefit until completing five years of service. *Id.* at 16-17, 22-29 (citing Bureau of Labor Statistics) (A-111-112, 114-115). Moreover, middle-aged and older employees subjected to a conversion from their traditional plan to a cash balance plan will typically receive a significantly smaller annuity at retirement (sometimes by as much as 50%) than if their employer had not converted their plan to a cash balance plan. *Id.* at 24-25 (A-115). For workers with equal salary and tenure, the worker who is oldest at the time of conversion will receive the lowest annuity at retirement. *Id.* at 25 (A-115-116).[4]

Additionally, due to the problematic methodology employed to compute the initial account balance at the time of conversion, employees may experience a period during which no new benefits accrue, a phenomenon frequently referred to as "wearaway." GAO Rept. at 28 (A-116-118). Wearaway

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[3] The GAO report was prepared after surveying 420 cash balance plans, interviewing numerous actuaries, pension consultants, and other pension experts, and performing sophisticated computerized modeling. *See* GAO Rept. at 4 (A-107-108).

[4] The reasons for these effects on older workers is explained in the GAO Rept.

tends to be longer for older workers. *Id.* Under GAO modeling, the basic cash balance plan generated a wearaway period ranging from two years for a thirty-five-year-old worker to eleven years for a fifty-five-year-old worker. *Id.* In light of the harsh effect a conversion has on middle-aged and older workers relative to younger workers, there has been a virtual avalanche of criticism lodged against cash balance plans that they discriminate against older workers, prompting investigation by the EEOC. *Id.* at 9 (A-110). In short, while cash balance plans *may* benefit *some* short-service, mobile, employees, these same plans generally reduce benefits payable to middle-aged and older employees.

Factual Background

Mr. Lyons' Participation in the Plan

From 1965 until approximately 1990, Mr. Lyons was employed as a paper inspector and paper tester for Great Northern Nekoosa Corporation ("Great Northern"). In 1990, Georgia-Pacific Corporation ("Georgia-Pacific") acquired Great Northern. As a result, Great Northern's pension plan merged with Georgia-Pacific's pension plan (the Plan), and Mr. Lyons became a participant in the Plan.

Plan Features

Like other cash balance plans, the Plan establishes a *bookkeeping* account for each participant (the "Personal Account") which is credited monthly with (1) service credits, a specified percentage of the participant's monthly pay; and (2) interest credits, a specified rate of interest. Plan at §§1.32, 3.1, 3.2 (A-123, 125). The interest crediting rate, referred to as the Periodic Adjustment Percentage, equals the PBGC twelve-month average "immediate" annuity rate for the calendar year preceding the year in which the interest credit is made plus .75%, divided by twelve (to obtain the monthly rate). Plan at

§3.5 (A-126).[5]

Although service credits cease when the participant separates from employment, interest credits continue until the participant's Benefit Commencement Date. Plan at §§ 3.2 and 3.5(b) (A-125, 126). For an annuity benefit, the Benefit Commencement Date is the date the annuity is payable. Plan at §1.5 (A-123). Thus, if the participant is entitled to an annuity at age 65, interest credits continue until age 65.

Under the Plan, a participant who separates from Georgia-Pacific with at least five years of service is entitled to a "Vested Benefit" equal to the "Accrued Benefit." Plan at §4.5 (A-126). The Accrued Benefit is a monthly annuity commencing on the participant's "Normal Retirement Date," computed by dividing the credits to the participant's Personal Account on that date by the "applicable factor" from Section A of Appendix A to the Plan. Plan at §1.1 (A-122). Normal Retirement Date is the date the participant attains age 65, and the factor at age 65 is 210. *See* Plan at §1.29 and Appendix A, Section A (A-123, 130). Thus, under the Plan, the Accrued Benefit is a monthly annuity commencing at age 65, computed by dividing the age 65 account balance by 210. This formulation of the Accrued Benefit as an annuity commencing at age 65 tracks ERISA's definition of the term "accrued benefit": "the individual's accrued benefit determined under the plan . . . expressed in the form of an annual benefit commencing at normal retirement age." 29 U.S.C. §1002(23) (A-3).

In lieu of the age 65 annuity benefit, a vested participant may elect a lump sum equal to the amount credited to his/her Personal Account as of the month preceding the Benefit Commencement Date. Plan at §6.4(a), Option C: Lump Sum Payment (A-131). With respect to a lump sum, Benefit Commencement Date means "the first date on which all events

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[5] PBGC is the acronym for Pension Benefit Guaranty Corporation, a governmental entity created to ensure that participants receive their pension benefits. 29 U.S.C. §1302(a) (A-15).

have occurred that entitle the participant to payment under [the] Plan." Plan at §1.5 (A-123). For a Vested Benefit, those events are (1) separation from Georgia-Pacific with at least 5 years of service, and (2) proper completion and submission of a "Qualified Election" form, waiving the annuity form of benefit and electing, instead, a lump sum. Plan at §§1.38, 4.5, 6.3(e), 6.4 (A-123, 126-127).[6]

Mr. Lyons' Administrative Claim

In January 1991, at the age of 49, Mr. Lyons separated from Georgia-Pacific. As Mr. Lyons had completed over 5 years of service (in fact, over 25 years of service), he was entitled to a Vested Benefit equal to the Accrued Benefit under the Plan, the annuity commencing at age 65. *See again* Plan at §§1.1, 1.29, and 4.5 (A-122, 123, 126). In November 1992, Mr. Lyons elected to receive his Accrued Benefit in an *optional* lump sum form, payable immediately, as was permitted under the Plan. Mr. Lyons received his lump sum distribution in January 1993.

Mr. Lyons subsequently discovered that his lump sum was less than the amount required under ERISA §203(e)(2) and TR 1.417(e)-1(d). In response to Mr. Lyons' administrative claim to recover the shortfall, Georgia-Pacific admitted that it made no attempt to comply with the present value rules under TR 1.417(e)-1(d), and that it simply distributed to Mr. Lyons an amount equal to his hypothetical account balance. *See* Letter from Georgia-Pacific to Paul Holzman, dated April 17, 1996 (A-134). If petitioners had complied with the present value rule under TR 1.417(e)-1(d), Mr. Lyons would have received $49,341.83, not $36,109.15, or 36.6% more than the amount petitioners distributed as his entire accrued benefit.

Georgia-Pacific subsequently affirmed its denial of Mr.

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[6] Thus, the Benefit Commencement Date for a lump sum is the date the participant is entitled to the benefit, whereas the Benefit Commencement Date for an annuity is the date the annuity is payable. *See again* Plan at §1.5 (A-123).

Lyons' claim. Having exhausted his administrative remedies, Mr. Lyons filed the instant class action against petitioners, alleging a single count: Violation of ERISA §203(e)(2).

Applicable Statutes, TRs and Other Regulatory Authority

As discussed, ERISA §203(e)(2) requires that the present value of any "nonforfeitable benefit" be no less than the present value of such benefit determined utilizing the interest rate set forth in the statute. 29 U.S.C. §1053(e) (A-5, 6). ERISA §3002(c) states that TRs promulgated under Code §§410(a), 411 and 412 (relating to minimum participation, vesting and funding standards, respectively) apply equally to the minimum participation, vesting and funding standards under ERISA. 29 U.S.C. §1202(c) (A-15). TR 1.411(a)-11(d), promulgated under Code §411, provides that in determining the present value of *any* accrued benefit, the plan must apply the valuation rules set forth in Code §417(e) and TR 1.417(e)-1(d). 26 C.F.R. §1.411(a)-11(d)(A-33). Because TR 1.411(a)-11(d) and ERISA §203(e) both govern minimum vesting requirements, it follows that the valuation rules under TR 1.411(a)-11(d), incorporating the valuation rules in Code §417(e) and TR 1.417(e)-1(d), apply equally to ERISA §203(e).

Like ERISA §203(e), TR 1.417(e)-1(d) requires the present value of a participant's accrued benefit to be no less than the amount computed utilizing the statutory interest rate. 26 C.F.R. §1.417(e)-1(d) (A-35, 36). Consistent with this requirement, TR 1.417(e)-1(d) explains that any optional lump sum must be no less than the present value of the participant's "normal retirement benefit." *Id.*

ERISA §3(22) and Code §411(a)(9) define "normal retirement benefit" as the greater of the early retirement benefit under the plan, or the benefit under the plan commencing at normal retirement age. 29 U.S.C. §1002(22) (A-3); 26 U.S.C. §411(a)(9) (A-20). Mr. Lyons was ineligible for, and did not elect to receive, an early retirement benefit. Rather, Mr. Lyons elected an immediate distribution of his Accrued Benefit, the annuity commencing at age 65.

Therefore, in computing Mr. Lyons' lump sum, petitioners were required to determine his normal retirement benefit (the annuity commencing at age 65), and then discount that annuity to present value utilizing an interest rate no greater than the rate specified in ERISA §203(e). Petitioners performed neither of these calculations, and, instead, simply distributed to Mr. Lyons' an amount equal to his hypothetical account balance. *See again* Letter from Georgia-Pacific to Paul Holzman (A-134).

As noted, the Accrued Benefit under the Plan is an annuity commencing at age 65, determined by dividing the age 65 account balance by an annuity factor of 210. Plan at §1.1 (A-122) and Appendix A, Section A (A-130). Although the Plan conditions service credits on continued service, it does not condition interest credits on continued service, as interest credits are payable until the Benefit Commencement Date. With respect to an annuity, the Benefit Commencement Date is the date the annuity is payable. Plan at §1.5 (A-123). Thus, *under the terms of the Plan*, interest credits to age 65 constitute part of the participant's Accrued Benefit. Any doubt that this is the case is readily dismissed by IRS Notice 96-8 which reviews the foregoing valuation rules in the context of "frontloaded" cash balance plans (those that do not condition interest credits on continued service). Notice 96-8 (A-51-55).

Notice 96-8 also explains that where a cash balance plan's interest crediting rate exceeds the statutory discount rate, distribution of an amount equal to the participant's account balance as the entire accrued benefit will (1) result in an underpayment of the participant's benefit entitlement; (2) violate the anti-forfeiture rules under Code §411(a) and TR 1.411(a)-4T; and (3) violate the present value rule under Code §417(e).[7] Notice 96-8 (A-48-49). It is undisputed that the Plan's

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[7] The anti-forfeiture rules under the Code and ERISA ensure that employees have a nonforfeitable right to 100% of their vested accrued benefit. *See* 26 U.S.C. §411(a)(1), (2) (A-19); and 29 U.S.C. §1053(a) (1), (2) (A-4). TR 1.411(a)-4T reiterates this requirement and explains: "A right to an accrued benefit is considered to be nonforfeitable at a particular time if, at

crediting rate exceeded the statutory discount rate. Petitioners' distribution to Mr. Lyons of solely an amount equal to his account balance, therefore, violated the anti-forfeiture and present value rules.

Rulings Below

The district court ruled that TRs 1.411(a)-11(d) and 1.417(e)-1(d) unreasonably expanded the scope of ERISA §203(e), and, on that basis, granted petitioners' motion for summary judgment. Petition at 38a-53a. The Eleventh Circuit Court of Appeals reversed, finding that the TRs represented a reasonable construction of the statute. Petition at 1a-37a.

REASONS FOR DENYING THE PETITION

I. Both the Statutory Language and Legislative History Establish that the Interest Rate Restrictions in ERISA §203(e)(2) Were Intended to Apply to the Actual Lump Sum Distributed.

Statutory Language

In effect, the Petition asks this Court to excuse the Plan (and all other cash balance plans) from the present value rule under ERISA §203(e). Petitioners contend that the statutory interest rate restrictions in subparagrah (2) of the statute apply solely for the purpose of determining whether a lump sum can be distributed without the participant's consent.[8] Petition at

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that time and thereafter, it is an unconditional right. . . *[A] right which, at a particular time, is conditioned under the plan upon a subsequent event, subsequent performance, or subsequent forbearance which will cause the loss of such right is a forfeitable right at that time.*" 26 C.F.R. §1.411(a)-4T (emphasis added) (A-32).

[8] Contrary to petitioners' assertion, the Eleventh Circuit Court of Appeals did not "concede" that the statutory terms apply solely to nonconsensual distributions. Petition at 14 n.9.

14. An examination of the statutory language, however, reveals that the interest rate restrictions also apply for purposes of determining the minimum amount that may be distributed with respect to *any* lump sum, consensual or nonconsensual:

> *(e) Consent for distribution; present value; covered distributions*
>
> (1) If the present value of any *nonforfeitable benefit* with respect to a participant in a plan *exceeds* $3,500, the plan shall provide that *such* benefit may not be *immediately distributed* without the consent of the participant.
>
> (2)(A) For purposes of paragraph (1), the present value shall be calculated –
>
> (i) by using an interest rate no greater than the applicable interest rate if the vested accrued benefit (using such rate) is not in excess of $25,000, and
>
> (ii) by using an interest rate no greater than 120 percent of the applicable interest rate if the vested accrued benefit exceeds $25,000 (as determined under clause (i)).
>
> *In no event shall the present value determined under subclause (II)[sic] be less than $25,000.*
>
> (B) For purposes of subparagraph (A), the term "applicable interest rate" means the interest rate which would be used (as of the date of distribution) by the Pension Benefit Guaranty Corporation for purposes of determining the present value of a lump sum *distribution* on plan termination.

29 U.S.C. §1053(e)(1986-Dec. 8, 1994) (emphasis added) (A-5). Petitioners' attempt to limit the interest rate restrictions to the determination of whether consent is required defies both logic and any reasonable construction of the statute. In view of the minimum *$25,000* distribution under the 120% rates, Congress

clearly did not intend ERISA §203(e)(2) to apply solely for purposes of making the consent determination. If Congress had intended that result, it would have (1) set the threshold for utilization of the 120% rates at $3,500, not $25,000; and (2) made the minimum distribution under the 120% rates $3,500, not $25,000.

Even without the $25,000 language, however, it is evident that the statutory interest rate restrictions are intended to apply to computation of the actual lump sum *distributed*. ERISA §203(e) is entitled "Consent for distribution; present value; covered distributions." This tri-part heading signifies that ERISA §203(e) addresses three matters: (1) the present value computation (2) of covered distributions [the "nonforfeitable benefits" referred to in the statute] *and* (3) the consent determination. Paragraph (1) of the statute requires the participant's consent to an *immediate* lump sum distribution if the present value of the participant's "nonforfeitable benefit" *exceeds* $3,500. Thus, paragraph (1) clearly addresses the "immediate distribution" of consensual lump sums *in excess* of $3,500. The "for purposes of paragraph (1)" language at the beginning of paragraph (2), therefore, necessarily means that Congress intended the statutory interest rate restrictions under paragraph (2) to apply to computation of the actual lump sum *distributed*.

Additional support for this conclusion is found in ERISA §205(g) and Code §417(e) which contain the same interest rate restrictions for computing present value. Paragraph (1) of these statutes states that plans may make an immediate lump sum distribution of the participant's annuity benefit if the present value does not exceed $3,500. 29 U.S.C. §1055(g)(1986-Dec. 8, 1994)(A-10); Code §417(e)(1986-Dec. 8, 1994) (A-22). Paragraph (2) provides that a plan may immediately distribute the present value of a participant's annuity benefit in excess of $3,500 only with the participant's consent. *Id.* Lastly, paragraph (3), relating to the determination of present value, states that it applies for purposes of *both* paragraphs (1) *and* (2), and then reiterates the interest rate restrictions in ERISA §203(e)(2). Thus, the interest

rate restrictions for computing the present value of an annuity benefit unambiguously apply for purposes of computing consensual lump sum distributions *in excess* of $3,500.

Code §411(a)(11) also requires the present value of an annuity benefit to be computed using the interest rate restrictions set forth in ERISA §203(e). Subparagraph (11) of Code §411(a) and subparagraph (e) of ERISA §203(e) were added by §105 of the Retirement Equity Act of 1984 ("REA"). *See* Pub. L. 98-397, §105, 99 Stat. 1426 (Aug. 23, 1984) (A-74). REA §105 and Code §411(a)(11) are both headed "Restrictions on certain *mandatory* distributions." *Id.* (emphasis added). Since the required form of distribution from a defined benefit plan is an annuity unless the participant *elects* to waive the annuity form of benefit, distribution of a lump sum is "mandatory" only where the participant has consented to the distribution. Therefore, Congress could not have intended the interest rate restrictions to apply solely for the purpose of making the consent determination.

Legislative History

The legislative history of the foregoing statutes likewise confirms that the statutory interest rate restrictions were intended to apply for purposes of computing the actual lump sum distributed. From ERISA's inception in 1974, ERISA and the Code permitted "cash-outs" of accrued benefits with or without the employee's consent, although the nonconsensual amount, initially, could not exceed $1,750. *See* Pub. L. 93-406, §204(d) and §1012, 88 Stat. 829 (Sept. 2, 1974) (A-73). ERISA and the Code permitted small nonconsensual cash-outs in order to relieve plans from the administrative burden of carrying relatively insubstantial amounts of benefits on their books for lengthy periods. *See* H.R. Rep. No. 93-807 (Feb. 21, 1974) (A-89). Contrary to petitioners' assertions, Congress never intended to prescribe different discounting rules for voluntary and involuntary cash-outs. Rather, Congress envisioned that participants would receive the full "value" of their accrued benefit, irrespective of the reason for the cash-

out. *See* H.R. Conf. Rep. No. 93-1280 (Aug. 12, 1974) (A-89). When ERISA was enacted, however, it contained no guidance for determining such value.

Ten years later, Congress passed the REA which amended ERISA and the Code to "improve the delivery of retirement benefits and provide for greater equity under private pension plans for workers and their spouses and dependents . . ." Preamble to S. Rep. No. 98-575 (Aug. 2, 1984) (A-90). Consistent with this goal and with Congress's prior pronouncements that cash-outs would be based on the "value" of the accrued benefit, the REA added paragraph (e) to ERISA §203 and Code §417, paragraph (g) to ERISA §205, and subparagraph (11) to Code §411(a). *See* Pub. L. 98-397, §§103, 105, 203 and 205, 98 Stat. 1426 (Aug. 23, 1984) (A-74). These provisions increased the nonconsensual amount to $3,500, and specified that the maximum rate that could be utilized to compute the present value of a participant's accrued benefit was the rate that would be utilized by the PBGC in a plan termination context. *Id.* Significantly, the Senate Report to the legislation emphasizes that the lump sum *distributed* must be computed utilizing a rate no greater than the PBGC rate. *See* S. Rep. No. 98-575 (Aug. 2, 1984) (A-90).

With passage of the Tax Reform Act of 1986 ("TRA"), Congress reaffirmed its mandate that all single sum distributions must be computed in accordance with the interest rate restrictions in ERISA §203(e). As amended by the TRA, ERISA §§203(e) and 205(g), and Code §§411(a)(11) and 417(e), read much as they had under the REA, with two exceptions: (1) if the present value exceeded $25,000 after using the PBGC rate, the present value could be recomputed utilizing 120% of the PBGC rate; and (2) the present value determined using the 120% rate *could not be less than $25,000.* Pub. L. 99-514, §1139, 100 Stat. 2085 (Oct. 22, 1986) (A-80).

By establishing a floor of $25,000 after application of the 120% rate, the statute negates any possible inference that Congress intended to limit the prescribed rates to the consent determination. If Congress had intended those rates to apply to the consent determination, only, it would simply have

stated that the participant's consent was required whenever the present value exceeded $3,500, *and stopped right there.* Congress chose to *add,* however, that the present value could be recomputed utilizing 120% of the PBGC rate if the present value exceeded $25,000 (using only the PBGC rate), but that the minimum present value under the 120% rate must be at least $25,000.[9] This latter provision confirms Congress's intent that the interest rate restrictions govern computation of the amount actually *distributed,* and not strictly the determination of whether the participant must consent to the lump sum distribution. To conclude otherwise would render the $25,000 language mere surplusage, a result inconsistent with accepted principles of statutory construction.

Any doubt that Congress intended the statutory interest rate restrictions to apply to the actual amount of the lump sum distributed, and not simply for purposes of making the consent determination, dissolves completely when one considers the House Conference Report to the TRA. There, Congress used a hypothetical to explain the operation of the statute. Under the hypothetical, if the present value using the PBGC rate, only, is $50,000, but $47,000 using 120% of the PBGC rate, the minimum lump sum that may be *distributed* is $47,000. *See* H.R. Conf. Rep. No. 99-841 (Sept. 18, 1986) (A-91). Obviously, if the statutory interest rate restrictions applied solely to the consent determination, the Conference Committee would not have stated that the minimum *distribution* under the 120% rate was $47,000.

The TRA's formulation of ERISA §203(e) remained intact until 1994 when §767 of the Retirement Protection Act of 1994 ("RPA") (1) eliminated the $25,000 language from ERISA §§203(e) and 205(g) and Code §§411(a)(11) and 417(e); (2) substituted 30-year Treasury rates for the PBGC rates and added a standard mortality table; and (3) eliminated the

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[9] As held by the Eleventh Circuit, this provision, at a minium, creates an ambiguity as to the proper construction of the statute and, therefore, invites deference to the applicable TRs. Petition at 2a-27a.

redundancies in ERISA and the Code by stating these new actuarial assumptions in ERISA §205(g) and Code §417(e), only, and incorporating them by reference in ERISA §203(e) and Code §411(a)(11). Pub. L. 103-465, §767, 108 Stat. 4809, (Dec. 8, 1994) (A-82).[10] Congress headed RPA §767 "Determination of Present Value for Purposes of Restrictions on *Mandatory* Distributions" (emphasis added), signifying, again, that it intended the statutory interest rate restrictions to apply to consensual lump sums and computation of the actual lump sum *distributed*.[11] The House Report to the RPA restates this intent, and explains that the purpose of the interest rate restrictions is to ensure that plans will not use "unreasonably" high interest rates to reduce participants' lump sum benefits. *See* H.R. Rep. No. 103-632(II)(Aug. 26, 1994)(A-105).[12]

TRs 1.411(a)-11(d) and 1.417(e)-1(d) require the present value of any accrued benefit, including an optional lump sum, to be no less than the present value of the participant's normal retirement benefit (here, the annuity commencing at age 65) determined in accordance with the statutory interest rate restrictions. 26 C.F.R. §§1.411(a)-11(d) (A-33) and 1.417(e)-1(d)

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[10] Historically, the 30-year Treasury rates have been higher than the PBGC rates. Congress adopted the higher Treasury rates (which produce a smaller lump sum) because, at the time the RPA was enacted, many plans were under funded, severely stressing PBGC resources when they terminated. *See* H.R. Rep. No. 103-632(I) (July 29, 1994) (A-94). By eliminating the PBGC rate, including 120% of that rate for amounts in excess of $25,00, and substituting the generally higher Treasury rates for all lump sum distributions, Congress sought to simultaneously ease the funding burden on plans and improve the financial soundness of the PBGC. *Id.*

[11] Section 1071 of the Taxpayer Relief Act of 1997 increased the $3,500 threshold for nonconsensual lump sums to $5,000, but, again, noted that the statute related to "restrictions on certain *mandatory* distributions. Pub. L. 105-34, §1071, 111 Stat. 899 (Aug. 5, 1997) (emphasis added) (A-87).

[12] Eight years earlier, Congress expressed this same concern in proceedings concerning lump sums paid on plan termination. *See Statement on the Plan Termination and Reversion Control Act of 1985*, 131 Cong. Rec. E 2614 (June 6, 1985) (A-120).

(A-35, 36). As evident by now, TRs 1.411(a)-11(d) and 1.417(e)-1(d) simply reiterate and enforce Congressional intent expressed in ERISA §203(e) (as well as ERISA §205(g) and Code §§411(a)(11) and 417(e)). These TRs have remained substantially intact since 1988[13] without objection from Congress, and the courts have relied on the TRs in interpreting the statute.[14] Under these circumstances, TRs 1.411(a)-11(d) and 1.417(e)-1(d) are entitled to the force and effect of law.[15]

II. On Appeal Below, Petitioners Asserted that the Standard of Review for "All" Issues Was *De Novo*.

Petitioners contend that, under *Firestone*, the Eleventh Circuit Court of Appeals should have deferred to petitioners' interpretation of the Plan. On appeal below, however, petitioners asserted that the standard of review for "all" issues was *de novo*. *See* Appellees' Brief at 14. Moreover, in *Firestone*, this Court expressly declined to state the standard of review

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[13] In fact, the precursor to TR 1.417(e)-1(d)--temporary TR 1.417(e)-1T--was promulgated in 1985 (A-33).

[14] *See Rybarczyk v. TRW, Inc.*, 2000 U.S. App. LEXIS 33360 *4-9, 23-24 (6th Cir. Dec. 21, 2000); *Esden v. Bank of Boston*, 229 F.3d 154, *passim* (2nd Cir. 2000); *Piggly Wiggly Southern, Inc. v. Pension Benefit Guaranty Corp.*, 1195 U.S. Dist. LEXIS 21934 *8-16 (N.D.Ala. Apr. 4, 1995), *aff'd*, 82 F.3d 430 (11th Cir. 1996); *Constantino v. TRW, Inc.*, 13 F.3d 969, 972-973, 978 (6th Cir. 1994); *Flo-Con Systs., Inc. v. Pension Benefit Guaranty Corp.*, 39 F. Supp. 2d 995, 999-1001 (D. Ill. 1998); *Kiefer v. Ceridian Corp.*, 976 F. Supp. 829, 833-835 (D.Minn. 1997) (also discussing temporary TR 1.417(e)-1T).

[15] *See National Muffler Dealers Ass'n. v. United States*, 440 U.S. 472, 477 (1979) (length of time and consistency of Commissioner's interpretation, as well as reliance on that interpretation, suggest TR carrying out Congressional mandate in a proper manner); *United States v. Correll*, 389 U.S. 299, 305 (1967) ("Treasury regulations and interpretations long continued without substantial change, applying to unamended or substantially reenacted statutes, are deemed to have received congressional approval and have the effect of law."); *Helvering, Commissioner of Internal Revenue v. Winmill*, 305 U.S. 79, 83 (1938)(same). *See also Davis v. United States*, 495 U.S. 472, 484 (1990) (longstanding TRs are entitled to "considerable weight").

for claims brought under ERISA's remedial provisions other than ERISA §502(a)(1)(B). *Firestone*, 489 U.S. 108. Mr. Lyons brought his ERISA §203(e)(2) claim under ERISA §502(a)(3), and, therefore, even if petitioners had argued for a deferential standard below, *Firestone* did not control.

Assuming, *arguendo*, that *Firestone* was somehow applicable, petitioners' denial of Mr. Lyons' claim would nevertheless have been reversed. In *Firestone*, this Court held that the standard of review (for claims under ERISA §502(a)(1)(B) for benefits *under the terms of the plan*) is *de novo* unless the plan granted the administrator discretion to construe "uncertain" terms, in which case the standard of review is arbitrary and capricious. *Firestone*, 489 U.S. at 111-112. The Plan *unambiguously* states that one of its principal purposes is to satisfy the requirements of the TRA "and subsequent legislation." Plan at p. 1 (A-122).

Through ERISA §203(e)(2), the TRA and "subsequent legislation" (discussed, *supra*) mandate that the present value of a participant's annuity benefit be no less than the present value determined in accordance with the statutory interest rate restrictions. Petitioners admitted they did not even attempt to comply with this requirement and, instead, simply distributed to Mr. Lyons an amount equal to his account balance. *See* Letter from Georgia-Pacific to Paul Holzman, dated April 17, 1996 (A-134). In light of the Plan's express purpose--to satisfy the requirements of the TRA and "subsequent legislation"--petitioners' admitted failure to even attempt compliance with the present value rules was patently arbitrary and capricious.

III. The Plan Provides the Interest Crediting Rule

After finding that TRs 1.411(a)-11(d) and 1.417(e)-1(d) reasonably construed ERISA §203(e), the Eleventh Circuit concluded that petitioners were required to (1) determine Mr. Lyons' normal retirement benefit (the annuity commencing at age 65); and (2) then discount that benefit to present value in accordance with the statutory interest rate restrictions. Petition at 26a-33a. It further held that, *under the terms of the*

Plan, step one required petitioners to project interest credits to Mr. Lyons' account balance to age 65 in order to determine the age 65 annuity benefit. *Id.*

Although petitioners insist that no Plan provision requires interest credits to be projected to age 65, even a cursory examination of the Plan establishes otherwise. The Plan states that (1) interest credits continue until the Benefit Commencement Date (Plan at §3.5(b)); (2) with respect to an annuity form of benefit, the Benefit Commencement Date is the date the annuity is payable (Plan at §1.5); (3) the Accrued Benefit is an annuity payable on the participant's Normal Retirement Date (Plan at §§1.1, 4.1, 6.2, 6.3); and (4) the participant's Normal Retirement Date is the date the participant attains the age of 65 (Plan at §1.29). *(See* A-122, 123, 126, 127).[16] Thus, *under the terms of the Plan*, interest credits *must* be projected to age 65 in order to determine the participant's accrued benefit/normal retirement benefit.[17]

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[16] Contrary to petitioners' assertions, the Plan does not define the accrued benefit as the participant's account balance "as of any given time." *See* Plan at §1.1 (A-122).

[17] Below, petitioners argued that interest crediting to age 65 was not required because (1) the Plan states that interest credits continue until the Benefit Commencement Date; and (2) for lump sums, the Benefit Commencement Date is the date of distribution. Appellees' Brief at 35-36. To the extent the Plan discontinues interest credits when the participant elects to receive the accrued benefit in a lump sum, such provision cannot be enforced. ERISA §203(a) and Code §411(a) expressly provide that participants possess a nonforfeitable right to 100% of their vested accrued benefit. 29 U.S.C. §1053(a)(1), (2)(A-4); 26 U.S.C. §411(a)(1), (2) (A-19). The Plan defines the accrued benefit as an annuity commencing at age 65. Plan at 1.1 (A-122). Therefore, any failure to compute interest credits to age 65 before discounting to present value necessarily causes a forfeiture of part of the participant's accrued benefit. Indeed, this point was stressed in IRS Notice 96-8 (A-52-53). *See also* 26 C.F.R. §1.411(a)-4T (A-32).

IV. Petitioners' Argument Under TR 1.411(a)-11(c)(2)(i) Was Never Discussed Below, and Is Based on a Mischaracterization of the Eleventh Circuit's Holding and Terms of the Plan.

Petitioners contend, for the first time, that (1) the Eleventh Circuit held that Mr. Lyons' "Accrued Benefit" under the Plan was $49,314.83 if he took an immediate distribution, but only $36,109.15 if he left his Accrued Benefit in the Plan; and (2) this creates a "significant detriment," in violation of TR 1.411(c)(2)(ii). Petition at 19. This Court can look high and low in the Eleventh Circuit's opinion and not find this holding. Furthermore, if a participant who separated from Georgia-Pacific elected to take his lump sum at a later date, rather than immediately, the lump sum would be larger, not smaller, because the annuity would be discounted for a shorter period of time. Thus, there exists no detriment at all to taking a lump sum distribution long after separation from employment, as opposed to immediately.[18] Either way, the participant will receive the present value of his/her accrued benefit, *assuming the Plan has complied with the present value rules.*

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[18] Petitioners made several other equally specious arguments below. For example, they argued that (1) Mr. Lyons accrued benefit was the amount credited to his account as of the date of his lump sum distribution, divided by a factor of 288 (the factor for an annuity payable at age 52, Mr. Lyons' age at the time of his lump sum distribution), (2) using this methodology Mr. Lyons should have received only $12,561 for his 25+ years of service, and (3) therefore, they overpaid Mr. Lyons approximately $23,500! Appellees' Brief at 40. Appendix A, Section A specifies the factors for computing an annuity benefit: 210 for the annuity payable at age 65, plus .50 for each month the *annuity* is paid earlier. Although the Plan permits participants under certain specified circumstances to *elect* payment of their annuity benefit before age 65, Mr. Lyons did not do so. Rather he elected an immediate lump sum distribution of his age 65 annuity benefit. Accordingly, petitioners were required to (1) project interest credits to age 65, (2) divide the age 65 account balance by 210 to determine Mr. Lyons' age 65 annuity benefit, and (3) then discount the age 65 benefit to present value in accordance with ERISA §203(e)(2).

V. Petitioners' "Unreasonableness" Argument Contradicts the Terms of the Plan.

Petitioners contend that requiring them to project interest credits to age 65 is "unreasonable" because such projection forward is not required under the law or terms of the Plan. Again, the Plan's own terms require interest credits to be computed to age 65 in order to determine the participant's Accrued Benefit. *See* Plan at §1.1, 1.5, 1.29 and Appendix A, Section A (A-122, 123, 130). Petitioners also erroneously assert that cash balance plans do not "estimate" mortality when computing a participant's accrued benefit, and, therefore, discounting to present value is inconsistent with the design of cash balance plans. Petition at 19-20. Ironically, Appendix A of the Plan reveals the falsity of this assertion. Appendix A provides the actuarial assumptions for determining the amount of the normal annuity benefit, as well as other *actuarially equivalent* annuities available under the plan upon election by the participant (A-130-131). Section D of Appendix A states that actuarial equivalence shall be determined using the 1971 Group Annuity [Mortality] Table (blended 80% male/20% female) and the PBGC immediate annuity rate (A-131). Likewise, the annuity factor for determining the normal annuity benefit payable at age 65 is 210, representing 210 monthly payments, or 17.5 years. Thus, the Plan "estimates" that participants will live to age 82.5.[19]

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[19] Petitioners also make the argument that application of the present value rules would permit participants to earn "double interest." Petition at 20 n. 12. Although interest credits must be projected to age 65 in order to determine the participant's accrued benefit, the age 65 benefit is discounted *back* to present value. Thus, much of the interest crediting is consumed by the interest discounting.

VI. The IRS Determination Letters Are Entitled to No Weight.

Petitioners contend that IRS determination letters ("DLs") received by the Plan "verify" its compliance with ERISA §203(e). Petition at 21-22. As an initial matter, 26 U.S.C. §6110(k)(3) (A-25) states that DLs "may not be used or cited as precedent." Furthermore, a DL is simply an insurance policy against tax disqualification. *See* IRS Publication 794 (A-41); and 26 C.F.R. §601.201(a) (a DL addresses only an individual's or organization's "status for tax purposes" and the "tax effects" of particular acts or transactions) (A-37). Moreover, even a favorable DL may be revoked or modified if it is found to be "in error or not in accord with the current view of the Service." 26 C.F.R. §601.201(l)(1),(4) (A-38-39). As importantly, TR 601.201 expressly states that DLs are limited to matters involving Code §401, 403(a), 405 and 501(a), and may not be issued with respect to other sections of the Code. 26 C.F.R. §601.201(o)(2) (A-40).

Consistent with the foregoing, the DLs received by the Plan did not address Code §§411 or 417 or any issue presented in this case. *See* Petition at 86a-91a. Likewise, the DLs caution that (1) they relate only to the status of the Plan under the Code, (2) are "not a determination regarding the effect of other Federal or local statutes," and (3) continued qualification depends upon the effect of the Plan "in operation." Petition at 86a, 87a, 89a, 90a. A note at the bottom of the DLs indicates the enclosure of IRS Publication 794. Petition at 87a, 91a. Publication 794 advises that a favorable DL (1) is "limited in scope"; (2) may have a "limited useful life"; (3) generally applies only to the *form* of the plan; and (4) is not applicable to the extent the plan does not qualify *in operation*. Publication 794 (A-41).[20] In view of these limitations, nearly all federal

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[20] Publication 794 suggests that the IRS's primary concern in reviewing a plan for DL purposes is determining whether the plan satisfies the minimum participation and coverage requirements and prohibits discrimination in favor of highly compensated employees (A-41).

courts that have considered the issue decline to defer to a DL *where it does not address the disputed issue(s), or the plan does not comply with applicable law "in operation."*[21] Not surprisingly, the Eleventh Circuit rejected the DLs because they did not address any issue in this case. Petition at 33a-34a.[22]

Lastly, petitioners claim that the IRS completed IRS Worksheet 2A, and, thereby, determined that the Plan satisfied Code §417(e). Petition at 22. Petitioners submit no proof of these alleged facts, and did not do so below. Accordingly, the blank Worksheet 2A petitioners now submit to this Court does not constitute evidence that the IRS determined that the Plan complied with Code §417(e). Indeed, if such evidence existed, one would think petitioners would have offered it below. Even if the IRS had completed Worksheet 2A, it would not defeat Mr. Lyons' right to challenge the propriety of

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[21] *See, e.g., Rybarczyk v. TRW, Inc.*, 235 F. 3d 975; 2000 U.S. App. LEXIS 3360 *25-27 (6th Cir. Dec. 21, 2000) *Esden v. Bank of Boston*, 229 F.3d 154, 175-177 (2nd Cir. 2000); *In re Gulf Pen. Litig.*, 764 F. Supp. 1149, 1172 (S.D. Tex. 1991), *aff'd sub nom Borst v. Chevron Corp.*, 36 F. 3d 1308 (5th Cir. 1994); *Hickey v. Chicago Truck Drivers, Helpers and Warehouse Workers Union*, 980 F.2d 465, 469 (7th Cir. 1992); *Flo-Con Systs., Inc. v. Pension Benefit Guaranty Corp.*, 39 F. Supp. 995, 1001-1002 (D.Ill. 1998); *Kiefer v. Ceridian Corp.*, 976 F. Supp. 829, 847 n.18 (D. Minn. 1997). *See also Christensen v. Harris County*, 529 U.S. 576, 631-632 (2000) (unlike agency regulations, agency interpretations in opinion letters not are not entitled to *Chevron* type deference).

[22] Below, petitioners nevertheless insisted that the IRS must have determined compliance with Code §§411 and 417 because the DLs state that the Plan is qualified under Code §401(a), and subparagraphs (7) and (11) of Code §401(a) require compliance with Code §§411 and 417. Appellees' Brief at 9-10, 13, 48-52. Code §401(a)(11) requires defined benefit plans to provided a "qualified joint and survivor annuity" and "qualified preretirement survivor annuity," "except as provided in [Code] section 417." 26 U.S.C. §401(a)(11)(A-17). Thus, Code §401(a)(11) addresses only the *form* of benefit that must be offered under the plan. Code §417(a), in turn, allows distribution of the annuity in an optional *form* if the participant so elects. 26 U.S.C. §417(a) (A-21). Code §401(a)(7) simply states that pension plans must comply with Code §411. 26 U.S.C. §401(a)(7) (A-17). Consequently, if a plan provision would violate §411 if implemented as written, the plan may nevertheless satisfy §401(a)(7) if it complies with §411 *in operation*.

petitioners' *operation* of the Plan, but would only render untenable any attempt by the IRS to disqualify the Plan.

VII. The "Safe Harbor" in Notice 96-8 Relates to Tax Qualification, Only.

As more fully explained in Mr. Lyons' Appeal Brief below (pp. 46-61), IRS Notice 96-8, issued January 16, 1996, emphasizes that cash balance plans are defined benefit plans (A-47, 50-51). As such, they must comply with the anti-forfeiture rules under Code §411(a)(1), (2) (A-19) and the present value rules under Code §417(e) (A-22, 23). Notice 96-8 also reviews the definition of "accrued benefit" under Code §411(a)(7) (A-20) and TR 1.411(a)-7(a) (A-32). Consistent with that definition, where a cash balance plan is "frontloaded," that is, does not condition interest credits on continued service (as here), interest credits to normal retirement age are part of the participant's accrued benefit. Notice 96-8 (A-50-56). Accordingly, interest credits must be projected to normal retirement age in order to determine the accrued benefit that will be discounted to present value. *Id.*[23] If the plan's crediting rate, however, exceeds the statutory discount rate, the present value will exceed the participant's account balance. *Id.* (A-48-49) Distribution of an amount equal to the participant's account balance as the entire accrued benefit in that instance would, therefore, violate the anti-forfeiture rules under Code

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[23] Notice 96-8 advises that the *proposed* crediting rates will be available to "front loaded" cash balance plans, only, because "backloaded" plans (i.e., those that condition interest credits on continued service) will not satisfy the benefit accrual rules under Code §411(b). Notice 96-8 (A-52). In the district court, Georgia-Pacific submitted the affidavit of its Chief Counsel, Benefits, who attested that Georgia-Pacific had adopted one of the *proposed* crediting rates in Notice 96-8. *See* Affidavit of James A. Talerico at ¶¶9 and 10 (A-138). *See also* June 27, 1997 amendment to the Plan at ¶3 (A-132) (adding a new subparagraph (2) to §3.5 of the Plan to provide that the 30-year Treasury rate is the applicable crediting rate for Plan years after December 31, 1995). The fact that the Plan adopted one of the proposed crediting rates further confirms that it is "frontloaded."

§411(a) and the present value rules under Code §417(e). *Id.*

After reviewing the foregoing valuation rules, Notice 96-8 advises that the Treasury intends to promulgate regulations containing crediting rates that may be used by cash balance plans. Notice 96-8 (A-56-57). Based on historical data, the proposed rates are "assumed" to be no greater than the 30-year Treasury rate (the statutory rate now and when Notice 96-8 was issued). *Id.* (A-58). A cash balance plan that adopts one of these rates (*after* implementation in TRs) may distribute the account balance as the entire accrued benefit without fear of violating Code §§411(a) or 417(e). *Id.* (A-?).

Notice 96-8 concludes by advising that (1) the anticipated regulations with the proposed crediting rates will be effective *prospectively*; and (2) "for plan years beginning before the regulations are effective, a plan will not be *disqualified* for failing to satisfy section 411(a) or 417(e) if the amount of the distribution satisfied those sections based on a reasonable, good-faith interpretation of the applicable provisions of the Code, taking into account pre-existing guidance." (A-58). Accordingly, the Eleventh Circuit properly ruled that the "safe harbor" protected against disqualification only, and not against liability to plan participants for violating ERISA. *See* Petition at 30a n.28.[24]

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[24] Contrary to petitioners' assertions, the Eleventh Circuit did not hold that a plan could be in compliance with the Notice 96-8 "safe harbor" rates, and still be liable to participants for violating ERISA §203(e). As just discussed, the "safe harbor" expressly states that the anticipated regulations with the proposed crediting rates will be effective *prospectively*. Notice 96-8 (A-58). As a result, a plan that adopts one of the *proposed* crediting rates before it is implemented in a TR does so with some risk. Indeed, as petitioners themselves note, the yield curve on 3-month T-Bills has been uncharacteristically high the past 5 years, perhaps explaining why the Treasury has not adopted that rate or any of the other *proposed* crediting rates. *See* http://www.federalreserve.gov/Releases (go to H.15, then Historical Data, then Treasury Constant Maturities, 3-month, monthly; and 30-year, monthly). Moreover, Notice 96-8 indicates that the *proposed* crediting rates will be set forth in regulations under Code §§411 and 417(e) (A-47). TRs under Code §411 are applicable to ERISA §203(e); and, therefore, if any *proposed* crediting rate is implemented in future TRs it will

VIII. Petitioners Had Considerable Notice of Their Obligations Under ERISA §203(e)(2).

Petitioners assert that, prior to Notice 96-8, cash balance plans had no notice that they were required to project interest credits to normal retirement age, and then discount to present value. Therefore, application of those requirements before issuance of the Notice violates the fair notice doctrine, or so the argument goes. Petition at 25-28.

In addition to discussing the *proposed* crediting rates, Notice 96-8 reviews the valuation rules applicable to *all* defined benefit plans, including Code §§411(a) and 417(e) and TRs 1.411(a)-7(a) and 1.411(a)-4T--authority that was in existence *years* before Mr. Lyons receive his distribution. As importantly, Notice 96-8 observes that (1) in September 1991, the Treasury issued TR 1.401(a)(4)-8(c)--a "safe harbor" regulation promulgated under Code §401(a)(4)--permitting cash balance plans to utilize the nondiscrimination rules available to defined contribution plans, but only if they comply with the *valuation* rules applicable to *defined benefit* plans; and (2) when regulations under Code §401(a)(4) were reissued in September 1993, this "safe harbor" was left unchanged. Notice 96-8 (A-49-50).

The "safe harbor" regulation referenced in Notice 96-8 was initially set forth in Treasury Decision ("TD") 8360, issued September 19, 1991. *See* TD 8360 (printing "final" regulations under §401(a)(4)) (A-60). *TD 8360 specifically informed cash balance plans that they must comply with the valuation rules under Code §417(e) and TR 1.417(e). Id.* (A-60). *See also* 26 C.F.R. §1.401(a)(4)-8(c) (1993-present) (reiterating 1991 "safe harbor") (A-27-31). Thus, sixteen months before Mr. Lyons received his distribution, petitioners received specific guidance informing them that, for purposes of the valuation rules, cash balance plans (1) *will* be treated like all other *defined benefit* plans; (2)

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be applicable to ERISA §203(e). Thus, the present value rules under ERISA will *continue* to be consistent with those under the Code.

must comply with Code §417(e) and TR 1.417(e)-1(d); and (3) *may not* distribute solely an amount equal to the participant's account balance if the plan's crediting rate exceeds the applicable discount rate. Clearly, the fair notice doctrine is not even remotely implicated in this case.

CONCLUSION

For the foregoing reasons, Mr. Lyons respectfully requests that the Petition be denied.

Respectfully submitted,

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ERISA STATUTES

29 U.S.C. §1001

§ 1001. Congressional findings and declaration of policy

(a) Benefit plans as affecting interstate commerce and the Federal taxing power

The Congress finds that the growth in size, scope, and numbers of employee benefit plans in recent years has been rapid and substantial; that the operational scope and economic impact of such plans is increasingly interstate; that the continued well-being and security of millions of employees and their dependents are directly affected by these plans; that they are affected with a national public interest; that they have become an important factor affecting the stability of employment and the successful development of industrial relations; that they have become an important factor in commerce because of the interstate character of their activities, and of the activities of their participants, and the employers, employee organizations, and other entities by which they are established or maintained; that a large volume of the activities of such plans are carried on by means of the mails and instrumentalities of interstate commerce; that owing to the lack of employee information and adequate safeguards concerning their operation, it is desirable in the interests of employees and their beneficiaries, and to provide for the general welfare and the free flow of commerce, that disclosure be made and safeguards be provided with respect to the establishment, operation, and administration of such plans; that they substantially affect the revenues of the United States because they are afforded preferential Federal tax treatment; that despite the enormous growth in such plans many employees with long years of employment are losing anticipated retirement benefits owing to the lack of vesting provisions in such plans; that owing to the inadequacy of current minimum standards, the soundness and stability of

plans with respect to adequate funds to pay promised benefits may be endangered; that owing to the termination of plans before requisite funds have been accumulated, employees and their beneficiaries have been deprived of anticipated benefits; and that it is therefore desirable in the interests of employees and their beneficiaries, for the protection of the revenue of the United States, and to provide for the free flow of commerce, that minimum standards be provided assuring the equitable character of such plans and their financial soundness.

(b) Protection of interstate commerce and beneficiaries by requiring disclosure and reporting, setting standards of conduct, etc., for fiduciaries

It is hereby declared to be the policy of this chapter to protect interstate commerce and the interests of participants in employee benefit plans and their beneficiaries, by requiring the disclosure and reporting to participants and beneficiaries of financial and other information with respect thereto, by establishing standards of conduct, responsibility, and obligation for fiduciaries of employee benefit plans, and by providing for appropriate remedies, sanctions, and ready access to the Federal courts.

(c) Protection of interstate commerce, the Federal taxing power, and beneficiaries by vesting of accrued benefits, setting minimum standards of funding, requiring termination insurance

It is hereby further declared to be the policy of this chapter to protect interstate commerce, the Federal taxing power, and the interests of participants in private pension plans and their beneficiaries by improving the equitable character and the soundness of such plans by requiring them to vest the accrued benefits of employees with significant periods of service, to meet minimum standards of funding, and by requiring plan termination insurance.

29 U.S.C. §1002(22)

(22) The term "normal retirement benefit" means the greater of the early retirement benefit under the plan, or the benefit under the plan commencing at normal retirement age. . .

29 U.S.C. §1002(23)

(23) The term "accrued benefit" means–

(A) in the case of a defined benefit plan, the individual's accrued benefit determined under the plan and, except as provided in section 1054(c)(3) of this title, expressed in the form of an annual benefit commencing at normal retirement age, or

(B) in the case of a plan which is an individual account plan, the balance of the individual's account.

* * *

29 U.S.C. §1002(24)

(24) The term "normal retirement age" means the earlier of–

(A) the time a plan participant attains normal retirement age under the plan, or

(B) the later of–

(i) the time a plan participant attains age 65, or

(ii) the 5th anniversary of the time a plan participant commenced participation in the plan.

* * *

29 U.S.C. §1002(34)

(34) The term "individual account plan" or "defined contribution plan" means a pension plan which provides for an individual account for each participant and for benefits based solely upon the amount contributed to the participant's account, and any income, expenses, gains and losses, and any

forfeitures of accounts of other participants which may be allocated to such participant's account.

29 U.S.C. §1002(35)

(35) The term "defined benefit plan" means a pension plan other than an individual account plan . . .

29 U.S.C. §1053(a)

Minimum vesting standards

(a) Nonforfeitability requirements

Each pension plan shall provide that an employee's right to his normal retirement benefit is nonforfeitable upon the attainment of normal retirement age and in addition shall satisfy the requirements of paragraphs (1) and (2) of this subsection.

(1) A plan satisfies the requirements of this paragraph if an employee's rights in his accrued benefit derived from his own contributions are nonforfeitable.

(2) A plan satisfies the requirements of this paragraph if it satisfies the requirements of subparagraph (A) or (B).

(A) A plan satisfies the requirements of this subparagraph if an employee who has completed at least 5 years of service has a nonforfeitable right to 100 percent of the employee's accrued benefit derived from employer contributions.

(B) A plan satisfies the requirements of this subparagraph if an employee has a nonforfeitable right to a percentage of the employee's accrued benefit derived from employer contributions determined under the following table:

Years of service:	**The nonforfeitable percentage is**
3	20
4	40
5	60

6.....	80
7 or more	100.

* * *

29 U.S.C. §1053(e)
(as formulated from 1986 to December 8, 1994)

(e) Consent for distribution; present value; covered distributions.

(1) If the present value of any nonforfeitable benefit with respect to a participant in a plan exceeds $3,500, the plan shall provide that such benefit may not be immediately distributed without the consent of the participant.

(2)(A) For purposes of paragraph (1), the present value shall be calculated–

(i) by using an interest rate no greater than the applicable interest rate if the vested accrued benefit (using such rate) is not in excess of $25,000, and

(ii) by using an interest rate no greater than 120 percent of the applicable interest rate if the vested accrued benefit exceeds $25,000 (as determined under clause (i)).

In no event shall the present value determined under subclause (II) [sic] be less than $25,000.

(B) For purposes of subparagraph (A), the term "applicable interest rate" means the interest rate which would be used (as of the date of distribution) by the Pension Benefit Guaranty Corporation for purposes of determining the present value of a lump sum distribution on plan termination.

* * *

29 U.S.C. §1053(e)
(as formulated after December 8, 1994)

(e) Consent for distribution; present value; covered distributions.

(1) If the present value of any nonforfeitable benefit with respect to a participant in a plan exceeds $ 3,500 [after 1997, $5,000], the plan shall provide that such benefit may not be immediately distributed without the consent of the participant.

(2) For purposes of paragraph (1), the present value shall be calculated in accordance with section 205(g)(3).

29 U.S.C. §1055(a)-(e)

§ 1055. Requirement of joint and survivor annuity and preretirement survivor annuity

(a) Required contents for applicable plans

Each pension plan to which this section applies shall provide that--

(1) in the case of a vested participant who does not die before the annuity starting date, the accrued benefit payable to such participant shall be provided in the form of a qualified joint and survivor annuity, and

(2) in the case of a vested participant who dies before the annuity starting date and who has a surviving spouse, a qualified preretirement survivor annuity shall be provided to the surviving spouse of such participant.

(b) Applicable plans

(1) This section shall apply to--

(A) any defined benefit plan,

* * *

(c) Plans meeting requirements of section

(1) A plan meets the requirements of this section only if--

(A) under the plan, each participant--

(i) may elect at any time during the applicable election period to waive the qualified joint and survivor annuity form of benefit or the qualified preretirement survivor annuity form of benefit (or both), and

(ii) may revoke any such election at any time during the applicable election period, and

(B) the plan meets the requirements of paragraphs (2), (3), and (4).

(2) Each plan shall provide that an election under paragraph (1)(A)(i) shall not take effect unless--

(A) (i) the spouse of the participant consents in writing to such election, (ii) such election designates a beneficiary (or a form of benefits) which may not be changed without spousal consent (or the consent of the spouse expressly permits designations by the participant without any requirement of further consent by the spouse), and (iii) the spouse's consent acknowledges the effect of such election and is witnessed by a plan representative or a notary public, or

(B) it is established to the satisfaction of a plan representative that the consent required under subparagraph (A) may not be obtained because there is no spouse, because the spouse cannot be located, or because of such other circumstances as

the Secretary of the Treasury may by regulations prescribe.

Any consent by a spouse (or establishment that the consent of a spouse may not be obtained) under the preceding sentence shall be effective only with respect to such spouse.

* * *

(d) "Qualified joint and survivor annuity" defined

For purposes of this section, the term "qualified joint and survivor annuity" means an annuity--

(1) for the life of the participant with a survivor annuity for the life of the spouse which is not less than 50 percent of (and is not greater than 100 percent of) the amount of the annuity which is payable during the joint lives of the participant and the spouse, and

(2) which is the actuarial equivalent of a single annuity for the life of the participant.

Such term also includes any annuity in a form having the effect of an annuity described in the preceding sentence.

(e) "Qualified preretirement survivor annuity" defined

For purposes of this section--

(1) Except as provided in paragraph (2), the term "qualified preretirement survivor annuity" means a survivor annuity for the life of the surviving spouse of the participant if--

(A) the payments to the surviving spouse under such annuity are not less than the amounts which would be payable as a survivor annuity under the qualified joint and survivor annuity under the plan (or the actuarial equivalent thereof) if--

(i) in the case of a participant who dies after the date on which the participant attained the earliest retirement age, such participant had retired with an immediate qualified joint and survivor annuity on the day before the participant's date of death, or

(ii) in the case of a participant who dies on or before the date on which the participant would have attained the earliest retirement age, such participant had--

(I) separated from service on the date of death,

(II) survived to the earliest retirement age,

(III) retired with an immediate qualified joint and survivor annuity at the earliest retirement age, and

(IV) died on the day after the day on which such participant would have attained the earliest retirement age, and

(B) under the plan, the earliest period for which the surviving spouse may receive a payment under such annuity is not later than the month in which the participant would have attained the earliest retirement age under the plan.

In the case of an individual who separated from service before the date of such individual's death, subparagraph (A)(ii)(I) shall not apply.

(2) In the case of any individual account plan or participant described in subparagraph (B) or (C) of subsection (b)(1) of this section, the term "qualified preretirement survivor annuity" means an annuity for the life of the surviving spouse the actuarial equivalent of which is not less than 50 percent of the portion of the account balance of the participant (as of the date of death) to which the participant had a nonforfeitable right (within the meaning of section 1053 of this title).

(3) For purposes of paragraphs (1) and (2), any security interest held by the plan by reason of a loan outstanding to the participant shall be taken into account in determining the amount of the qualified preretirement survivor annuity.

29 U.S.C. §1055(g)
(as formulated from 1986 to December 8, 1994)

(g) Distribution of present value of annuity; written consent; determination of present value.

(1) A plan may provide that the present value of a qualified joint and survivor annuity or a qualified preretirement survivor annuity will be immediately distributed if such value does not exceed $ 3,500. No distribution may be made under the preceding sentence after the annuity starting date unless the participant and the spouse of the participant (or where the participant has died, the surviving spouse) consent in writing to such distribution.

(2) If--

(A) the present value of the qualified joint and survivor annuity or the qualified preretirement survivor annuity exceeds $ 3,500, and

(B) the participant and the spouse of the participant (or where the participant has dies, the surviving spouse) consent in writing to the distribution,

the plan may immediately distribute the present value of such annuity.

(3) (A) For purposes of paragraphs (1) and (2), the present value shall be calculated-

(i) by using an interest rate no greater than the applicable interest rate if the vested accrued benefit (using such rate) is

not in excess of $ 25,000, and

(ii) by using an interest rate no greater than 120 percent of the applicable interest rate if the vested accrued benefit exceeds $ 25,000 (as determined under clause (i)).

In no event shall the present value determined under subclause (II) [sic, clause (ii)] be less than $ 25,000.

(B) For purposes of subparagraph (A), the term "applicable interest rate" means the interest rate which would be used (as of the date of the distribution) by the Pension Benefit Guaranty Corporation for purposes of determining the present value of a lump sum distribution on plan termination.

29 U.S.C. §1055(g)
(as formulated after December 8, 1994)

(g) Distribution of present value of annuity; written consent; determination of present value.

(1) A plan may provide that the present value of a qualified joint and survivor annuity or a qualified preretirement survivor annuity will be immediately distributed if such value does not exceed $ 3,500 [after 1997, "the dollar limit under section 203(e)(1)"]. No distribution may be made under the preceding sentence after the annuity starting date unless the participant and the spouse of the participant (or where the participant has died, the surviving spouse) consent in writing to such distribution.

(2) If--

(A) the present value of the qualified joint and survivor annuity or the qualified preretirement survivor annuity *exceeds* $ 3,500 [after 1997, "the dollar limit under section 203(e)(1)"], and

(B) the participant and the spouse of the participant (or where the participant has died, the surviving spouse) consent in writing to the distribution,

the plan may immediately distribute the present value of such annuity.

(3) Determination of present value.

(A) In general.

(i) Present value. Except as provided in subparagraph (B), for purposes of paragraphs (1) and (2), the present value shall not be less than the present value calculated by using the applicable mortality table and the applicable interest rate.

(ii) Definitions. For purposes of clause (i)--

(I) Applicable mortality table. The term "applicable mortality table" means the table prescribed by the Secretary of the Treasury. Such table shall be based on the prevailing commissioners' standard table (described in section 807(d)(5)(A) of the Internal Revenue Code of 1986 used to determine reserves for group annuity contracts issued on the date as of which present value is being determined (without regard to any other subparagraph of section 807(d)(5) of such Code).

(II) Applicable interest rate. The term "applicable interest rate" means the annual rate of interest on 30-year Treasury securities for the month before the date of distribution or such other time as the Secretary of the Treasury may by regulations prescribe.

(B) Exception. In the case of a distribution from a plan that was adopted and in effect prior to the date of the enactment of the Retirement Protection Act of 1994 [enacted Dec. 8, 1994], the present value of any distribution made before the earlier

of--

(i) the later of when a plan amendment applying subparagraph (A) is adopted or made effective, or

(ii) the first day of the first plan year beginning after December 31, 1999,

shall be calculated, for purposes of paragraphs (1) and (2), using the interest rate determined under the regulations of the Pension Benefit Guaranty Corporation for determining the present value of a lump sum distribution on plan termination that were in effect on September 1, 1993, and using the provisions of the plan as in effect on the day before such date of enactment [Dec. 8, 1994] but only if such provisions of the plan met the requirements of section 205(g)(3) [this paragraph] as in effect on the day before such date of enactment.

29 U.S.C. §1081(a)

§ 1081. Coverage

(a) Plans excepted from applicability of this part [Part 3–Funding]

This Part shall apply to any employee pension benefit plan described in section 1003(a) of this title [plans established by employers engaged in commerce or in an industry or activity affecting commerce], (and not exempted under section 1003(b) of this title) [governmental and church plans, plans maintained solely to comply with workers' compensation laws, foreign plans, and unfunded excess benefit plans], other than–[lists welfare benefit, insurance and other plans, but not defined benefit plans]

* * *

(material in brackets added).

29 U.S.C. §1082(a), (b)

§ 1082. Minimum funding standards

(a) Avoidance of accumulated funding deficiency

(1) Every employee pension benefit plan subject to this part shall satisfy the minimum funding standard (or the alternative minimum funding standard under section 1085 of this title) for any plan year to which this part applies. A plan to which this part applies shall have satisfied the minimum funding standard for such plan for a plan year if as of the end of such plan year the plan does not have an accumulated funding deficiency.

* * *

(b) Funding standard account

(1) Each plan to which this part applies shall establish and maintain a funding standard account. Such account shall be credited and charged solely as provided in this section.

* * *

29 U.S.C. §1132(a)(1)-(3)

§ 1132. Civil enforcement

(a) Persons empowered to bring a civil action

A civil action may be brought–

(1) by a participant or beneficiary–

(A) for the relief provided for in subsection (c) of this section, or

(B) to recover benefits due to him under the terms of his plan, to enforce his rights under the terms of the plan, or to clarify his rights to future benefits under the terms of the plan;

(2) by the Secretary, or by a participant, beneficiary or

fiduciary for appropriate relief under section 1109 of this title;

(3) by a participant, beneficiary, or fiduciary (A) to enjoin any act or practice which violates any provision of this subchapter or the terms of the plan, or (B) to obtain other appropriate equitable relief (i) to redress such violations or (ii) to enforce any provisions of this subchapter or the terms of the plan;

29 U.S.C. §1202(c)

(c) Extended application of regulations prescribed by Secretary of the Treasury relating to minimum participation standards, minimum vesting standards, and minimum funding standards

Regulations prescribed by the Secretary of the Treasury under sections 410(a), 411, and 412 of Title 26 (relating to minimum participation standards, minimum vesting standards, and minimum funding standards, respectively) shall also apply to the minimum participation, vesting and funding standards set forth in parts 2 and 3 of subtitle B of subchapter I of this chapter. . . .

29 U.S.C. §1302(a)

§ 1302. Pension Benefit Guaranty Corporation

(a) Establishment within Department of Labor

There is established within the Department of Labor a body corporate to be known as the Pension Benefit Guaranty Corporation. In carrying out its functions under this subchapter, the corporation shall be administered by the chairman of the board of directors in accordance with policies established by the board. The purposes of this subchapter, which are to be carried out by the corporation, are–

(1) to encourage the continuation and maintenance of voluntary private pension plans for the benefit of their participants,

(2) to provide for the timely and uninterrupted payment of pension benefits to participants and beneficiaries under plans to which this subchapter applies, and

(3) to maintain premiums established by the corporation under section 1306 of this title at the lowest level consistent with carrying out its obligations under this subchapter.

INTERNAL REVENUE CODE STATUTES

26 U.S.C. §401(a)(7), (11)

§401. Qualified pension, profit-sharing, and stock bonus plans

(a) Requirements for qualification.–A trust created or organized in the United States and forming part of a stock bonus, pension, or profit-sharing plan of an employer for the exclusive benefit of his employees or their beneficiaries shall constitute a qualified trust under this section–[listing design and operational requirements under subparagraphs (1) through (34)]

* * *

(7) A trust shall not constitute a qualified trust under this section unless the plan of which such trust is a part satisfies the requirements of section 411 (relating to minimum vesting standards).

* * *

(11) Requirement of joint and survivor annuity and preretirement survivor annuity.–

(A) In general.–In the case of any plan to which this paragraph applies, except as provided in section 417, a trust forming part of such plan shall not constitute a qualified trust under this section unless–

(i) in the case of a vested participant who does not dies before the annuity starting date, the accrued benefit payable to such participant is provided in the form of a qualified joint and survivor annuity, and

(ii) in the case of a vested participant who dies before the annuity starting date and who has a surviving spouse, a qualified preretirement survivor annuity is provided to the surviving spouse of such participant.

26 U.S.C. §402(a)

§402. Taxability of beneficiary of employees' trust

(a) Taxability of beneficiary of exempt trust. Except as otherwise provided in this section, any amount actually distributed to any distributee by any employees' trust described in section 401(a) which is exempt from tax under section 501(a) shall be taxable to the distributee, in the taxable year of the distributee in which distributed, under section 72 (relating to annuities).

26 U.S.C. §404(a)

§404. Deduction for contributions of an employer to an employees' trust or annuity plan and compensation under a deferred-payment plan

(a) General rule.–If contributions are paid by an employer to or under a stock bonus, pension, profit-sharing, or annuity plan, or if compensation is paid or accrued on account of any employee under a plan deferring the receipt of such compensation, such contributions or compensation shall not be deductible under this chapter; but, if they would otherwise be deductible, they shall be deductible under this section, subject, however, to the following limitations as to the amounts deductible in any year.

(1) Pension trusts.--

(A) In general.–In the taxable year when paid, if the contributions are paid into a pension trust, and if such taxable year ends within or with a taxable year of the trust for which the trust is exempt under section 501(a), in an amount determined as follows: [lists the amounts deductible under various circumstances]

* * *

26. U.S.C. §411(a)(1), (2)

§ 411 Minimum vesting standards.

(a) General rule. A trust shall not constitute a qualified trust under section 401(a) unless the plan of which such trust is a part provides that an employee's right to his normal retirement benefit is nonforfeitable upon the attainment of normal retirement age (as defined in paragraph (8)) and in addition satisfies the requirements of paragraphs (1), (2), and (11) of this subsection and the requirements of subsection (b)(3), and also satisfies, in the case of a defined benefit plan, the requirements of subsection (b)(1) and, in the case of a defined contribution plan, the requirements of subsection (b)(2).

(1) Employee contributions. A plan satisfies the requirements of this paragraph if an employee's rights in his accrued benefit derived from his own contributions are nonforfeitable.

(2) Employer contributions. A plan satisfies the requirements of this paragraph if it satisfies the requirements of subparagraph (A), (B), or (C).

(A) 5-year vesting. A plan satisfies the requirements of this subparagraph if an employee who has completed at least 5 years of service has a nonforfeitable right to 100 percent of the employee's accrued benefit derived from employer contributions.

Years of service:	The nonforfeitable percentage is:
3	20
4	40
5	60
6	80
7 or more	100.

* * *

26 U.S.C. §411(a)(7), (9)

(7) Accrued benefit.--

(A) In general.-- For purposes of this section, the term "accrued benefit" means-

(i) in the case of a defined benefit plan, the employee's accrued benefit determined under the plan and, except as provided in subsection (c)(3), expressed in the form of an annual benefit commencing at normal retirement age, or

(ii) in the case of a plan which is not a defined benefit plan, the balance of the employee's account.

* * *

(9) Normal retirement benefit.-For purposes of this section, the term "normal retirement benefit" means the greater of the early retirement benefit under the plan, or the benefit under the plan commencing at normal retirement age. . . .

26 U.S.C. §411(a)(11)
(as formulated from 1986 to December 8, 1994)

(11) Restrictions on certain mandatory distributions.

(A) In general. If the present value of any nonforfeitable accrued benefit exceeds $ 3,500, a plan meets the requirements of this paragraph only if such plan provides that such benefit may not be immediately distributed without the consent of the participant.

(B) Determination of present value.

(i) In general.--For purposes of subparagraph (A), the present value shall be calculated -

(I) by using an interest rate no greater than the applicable interest rate if the vested accrued benefit (using such rate) is not in excess of $ 25,000, and

(II) by using an interest rate no greater than 120 percent of the applicable interest rate if the vested accrued benefit exceeds $ 25,000 (as determined under subclause (I)).

In no event shall the present value determined under subclause (II) be less than $ 25,000.

(ii) Applicable interest rate.--For purposes of clause (i), the term "applicable interest rate" means the interest rate which would be used (as of the date of the distribution) by the Pension Benefit Guaranty Corporation for purposes of determining the present value of a lump sum distribution on plan termination.

* * *

26 U.S.C. §411(a)(11)
(as formulated after December 8, 1994)

(11) Restrictions on certain mandatory distributions.

(A) In general.--If the present value of any nonforfeitable accrued benefit exceeds $ 3,500 [after 1997, $5,000], a plan meets the requirements of this paragraph only if such plan provides that such benefit may not be immediately distributed without the consent of the participant.

(B) Determination of present value.--For purposes of subparagraph (A), the present value shall be calculated in accordance with section 417(e)(3).

* * *

26 U.S.C. §417(a)

(a) Election to waive qualified joint and survivor annuity or qualified preretirement survivor annuity.--

(1) In general.-A plan meets the requirements of section 401(a)(11) only if-

(A) under the plan, each participant-

(i) may elect at any time during the applicable election period to waive the qualified joint and survivor annuity form of benefit or the qualified

preretirement survivor annuity form of benefit (or both), and

(ii) may revoke any such election at any time during the applicable election period, and

(B) the plan meets the requirements of paragraphs (2), (3), and (4) of this subsection.

(2) **Spouse must consent to election.**-- . . .

* * *

26 U.S.C. §417(e)
(as formulated from 1986 to December 8, 1994)

(e) Restrictions on cash-outs.

(1) Plan may require distribution if present value not in excess of $ 3,500. A plan may provide that the present value of a qualified joint and survivor annuity or a qualified preretirement survivor annuity will be immediately distributed if such value does not exceed $ 3,500. No distribution may be made under the preceding sentence after the annuity starting date unless the participant and the spouse of the participant (or where the participant has died, the surviving spouse) consents in writing to such distribution.

(2) Plan may distribute benefit in excess of $3,500 only with consent. If-

(A) the present value of the qualified joint and survivor annuity or the qualified preretirement survivor annuity exceeds $ 3,500, and

(B) the participant and the spouse of the participant (or where the participant has died, the surviving spouse) consent in writing to the distribution, the plan may immediately distribute the present value of such annuity.

(3) Determination of present value.

(A) In general. For purposes of paragraphs (1) and (2), the present value shall be calculated-

(i) by using an interest rate no greater than the applicable interest rate if the vested accrued benefit (using such rate) is

not in excess of $ 25,000, and

(ii) by using an interest rate no greater than 120 percent of the applicable interest rate if the vested accrued benefit exceeds $ 25,000 (as determined under clause (i)).

In no event shall the present value determined under clause (ii) be less than $25,000.

(B) Applicable interest rate. For purposes of subparagraph (A), the term "applicable interest rate" means the interest rate which would be used (as of the date of the distribution) by the Pension Benefit Guaranty Corporation for purposes of determining the present value of a lump sum distribution on plan termination.

26 U.S.C. §417(e)
(as formulated after December 8, 1994)

(e) Restrictions on cash-outs.

(1) Plan may require distribution if present value not in excess of $ 3,500 [after 1997, "dollar limit"]. A plan may provide that the present value of a qualified joint and survivor annuity or a qualified preretirement survivor annuity will be immediately distributed if such value does not exceed $ 3,500 [after 1997, "the dollar limit under section 411(a)(11)(A)"]. No distribution may be made under the preceding sentence after the annuity starting date unless the participant and the spouse of the participant (or where the participant has died, the surviving spouse) consents in writing to such distribution.

(2) Plan may distribute benefit in excess of $ 3,500 only with consent. If--

(A) the present value of the qualified joint and survivor annuity or the qualified preretirement survivor annuity exceeds $ 3,500 [after 1997, "the dollar limite under section 411(a)(11)(A)"], and

(B) the participant and the spouse of the participant (or

where the participant has died, the surviving spouse) consent in writing to the distribution,

the plan may immediately distribute the present value of such annuity.

(3) Determination of present value.

(A) In general.

(i) Present value. Except as provided in subparagraph (B), for purposes of paragraphs (1) and (2), the present value shall not be less than the present value calculated by using the applicable mortality table and the applicable interest rate.

(ii) Definitions. For purposes of clause (i)--

(I) Applicable mortality table. The term "applicable mortality table" means the table prescribed by the Secretary. Such table shall be based on the prevailing commissioners' standard table (described in section 807(d)(5)(A)) used to determine reserves for group annuity contracts issued on the date as of which present value is being determined (without regard to any other subparagraph of section 807(d)(5)).

(II) Applicable interest rate. The term "applicable interest rate" means the annual rate of interest on 30-year Treasury securities for the month before the date of distribution or such other time as the Secretary may by regulations prescribe,

(B) Exception. In the case of a distribution from a plan that was adopted and in effect before the date of the enactment of the Retirement Protection Act of 1994, the present value of any distribution made before the earlier of--

(i) the later of the date a plan amendment applying subparagraph (A) is adopted or made effective, or

(ii) the first day of the first plan year beginning after

December 31, 1999,

shall be calculated, for purposes of paragraphs (1) and (2), using the interest rate determined under the regulations of the Pension Benefit Guaranty Corporation for determining the present value of a lump sum distribution on plan termination that were in effect on September 1, 1993, and using the provisions of the plan as in effect on the day before such date of enactment; but only if such provisions of the plan met the requirements of section 417(e)(3) as in effect on the day before such date of enactment.

26 U.S.C. §501(a)

§501. Exemption from tax on corporations, certain trusts, etc.

(a) Exemption from taxation.–An organization described in subsection (c) or (d) or section 401(a) shall be exempt from taxation under this subtitle unless such exemption is denied under section 502 or 503.

* * *

26 U.S.C. §6110(k)(3)

§ 6110. Public inspection of written determinations.

* * *

(b) Definitions. For purposes of this section–

(1) Written determination. The term "written determination" means a ruling, determination letter, technical advice memorandum, or Chief Counsel advice. . . .

* * *

(k) Special provisions.

* * *

(3) Precedential status. Unless the Secretary otherwise establishes by regulations, a written determination may not be used or cited as precedent.

* * *

TREASURY REGULATIONS

26 C.F.R. §1.401(a)(4)-8(c)(3)
(Sept. 3, 1991-present)

(3) Safe harbor testing method for cash balance plans--(i) General rule. A cash balance plan is a defined benefit plan that defines benefits for each employee by reference to the employee's hypothetical account. An employee's hypothetical account is determined by reference to hypothetical allocations and interest adjustments that are analogous to actual allocations of contributions and earnings to an employee's account under a defined contribution plan. Because a cash balance plan is a defined benefit plan, whether it satisfies section 401(a)(4) with respect to the equivalent amount of contributions is generally determined under paragraphs (c)(1) and (c)(2) of this section. However, a cash balance plan that satisfies each of the requirements in paragraphs (c)(3)(ii) through (xi) of this section is deemed to satisfy section 401(a)(4) with respect to an equivalent amount of contributions.

(ii) Plan requirements in general. The plan must be an accumulation plan. The benefit formula under the plan must provide for hypothetical allocations for each employee in the plan that satisfy paragraph (c)(3)(iii) of this section, and interest adjustments to these hypothetical allocations that satisfy paragraph (c)(3)(iv) of this section. The benefit formula under the plan must provide that these hypothetical allocations and interest adjustments are accumulated as a hypothetical account for each employee, determined in accordance with paragraph (c)(3)(v) of this section. **The plan must provide that an employee's accrued benefit under the plan as of any date is an annuity that is the actuarial equivalent of the employee's projected hypothetical account as of normal retirement age, determined in accordance with paragraph (c)(3)(vi) of this section. In addition, the plan must satisfy paragraphs (c)(3)(vii) through (xi) of this section (to the extent applicable) regarding optional forms of**

benefit, past service credits, post-normal retirement age benefits, certain uniformity requirements, and changes in the plan's benefit formula, respectively.

* * *

(iv) Interest adjustments to hypothetical allocations--(A) General rule. The plan benefit formula must provide that the dollar amount of the hypothetical allocation for each employee for a plan year is automatically adjusted using an interest rate that satisfies paragraph (c)(3)(iv)(B) of this section, compounded no less frequently than annually, for the period that begins with a date in the plan year and that ends at normal retirement age. This requirement is not satisfied if any portion of the interest adjustments to a hypothetical allocation are contingent on the employee's satisfaction of any requirement. Thus, for example, the interest adjustments to a hypothetical allocation must be provided through normal retirement age, even though the employee terminates employment or commences benefits before that age.

(B) Requirements with respect to interest rates. The interest rate must be a single interest rate specified in the plan that is the same for all employees in the plan for all plan years. The interest rate must be either a standard interest rate or a variable interest rate. If the interest rate is a variable interest rate, it must satisfy paragraph (c)(3)(iv)(C) of this section.

(C) Variable interest rates--(1) General rule. The plan must specify the variable interest rate, the method for determining the current value of the variable interest rate, and the period (not to exceed 1 year) for which the current value of the variable interest rate applies. Permissible variable interest rates are listed in paragraph (c)(3)(iv)(C)(2) of this section. Permissible methods for determining the current value of the variable interest rate are provided in paragraph (c)(3)(iv)(C)(3) of this section.

(2) Permissible variable interest rates. The variable interest rate specified in the plan must be one of the following--

(i) The rate on 3-month Treasury Bills,
(ii) The rate on 6-month Treasury Bills,
(iii) The rate on 1-year Treasury Bills,
(iv) The yield on 1-year Treasury Constant Maturities,
(v) The yield on 2-year Treasury Constant Maturities,
(vi) The yield on 5-year Treasury Constant Maturities,
(vii) The yield on 10-year Treasury Constant Maturities,
(viii) The yield on 30-year Treasury Constant Maturities, or
(ix) The single interest rate such that, as of a single age specified in the plan, the actuarial present value of a deferred straight life annuity of an amount commencing at the normal retirement age under the plan, calculated using that interest rate and a standard mortality table but assuming no mortality before normal retirement age, is equal to the actuarial present value, as of the single age specified in the plan, of the same annuity calculated using the section 417(e) rates applicable to distributions in excess of $25,000 (determined under § 1.417(e)-1(d)), and the same mortality assumptions.
(v) Hypothetical account--(A) Current value of hypothetical account. As of any date, the current value of an employee's hypothetical account must equal the sum of all hypothetical allocations and the respective interest adjustments to each such hypothetical allocation provided through the date for the employee under the plan's benefit formula (without regard to any interest adjustments provided under the plan's benefit formula for periods after that date).
(B) Value of hypothetical account as of normal retirement age. Under paragraph (c)(3)(vi) of this section, the value of an employee's hypothetical account must be determined as of normal retirement age in order to determine the employee's accrued benefit as of any date at or before normal retirement age. As of any date at or before normal retirement age, the value of an employee's hypothetical account as of normal retirement age must equal the sum of each hypothetical allocation provided through that date for the employee under the plan's benefit formula, plus the interest adjustments provided through normal retirement age on each of those hypothetical allocations for the

employee under the plan's benefit formula (without regard to any hypothetical allocations that might be provided after that date under the plan's benefit formula). If the interest rate specified in the plan is a variable interest rate, the plan must specify that the determination in the preceding sentence is made by assuming that the current value of the variable interest rate for all future periods is either the current value of the variable interest rate for the current period or the average of the current values of the variable interest rate for the current period and one or more periods immediately preceding the current period (not to exceed 5 years in the aggregate).

(vi) Determination of accrued benefit--(A) Definition of accrued benefit. The plan must provide that at any date at or before normal retirement age the accrued benefit (within the meaning of section 411(a)(7)(A)(i)) of each employee in the plan is an annuity commencing at normal retirement age that is the actuarial equivalent of the employee's hypothetical account as of normal retirement age (as determined under paragraph (c)(3)(v)(B) of this section). The separate benefit that each employee accrues for a plan year is an annuity that is the actuarial equivalent of the employee's hypothetical allocation for that plan year, including the automatic adjustments for interest through normal retirement age required under paragraph (c)(3)(iv) of this section.

(B) Normal form of benefit. The annuity specified in paragraph (c)(3)(vi)(A) of this section must provide an annual benefit payable in the same form at the same uniform normal retirement age for all employees in the plan. The annual benefit must be the normal retirement benefit under the plan (within the meaning of section 411(a)(9)) under the plan.

(C) Determination of actuarial equivalence. For purposes of this paragraph (c)(3)(vi) and paragraph (c)(3)(ix) of this section, actuarial equivalence must be determined using a standard mortality table and either a standard interest rate or the interest rate specified in the plan for making interest adjustments to hypothetical allocations. If the interest rate

used is the interest rate specified in the plan, and that rate is a variable interest rate, the assumed value of the variable interest rate for all future periods must be the same value that would be assumed for purposes of paragraph (c)(3)(v)(B) of this section. The same actuarial assumptions must be used for all employees in the plan.

* * *

(vii) Optional forms of benefit–

* * *

(C) Distributions subject to section 417(e). Except as otherwise required under section 415(b), **if the plan provides for a distribution alternative that is subject to the interest rate restrictions under section 417(e), the actuarial present value of the benefit paid to an employee under the distribution alternative must equal the nonforfeitable percentage (determined under the plan's vesting schedule) of the greater of the following two amounts–**

(1) The current value of the employee's hypothetical account as of the date the distribution commences, calculated in accordance with paragraph (c)(3)(v)(A) of this section.

(2) The actuarial present value (calculated in accordance with § 1.417(e)- 1(d)) of the employee's accrued benefit.

(D) Determination of actuarial present value. For purposes of this paragraph (c)(3)(vii), actuarial present value must be determined using a reasonable interest rate and mortality table. A standard interest rate and a standard mortality table are considered reasonable for this purpose.

* * *

(emphasis added).

26 C.F.R. § 1.411(a)-4T
("temporary" regulation, 1988 to present)

§ 1.411(a)-4T Forfeitures, suspensions, etc. (temporary)

(a) Nonforfeitability. Certain rights in an accrued benefit must be nonforfeitable to satisfy the requirements of section 411(a). This section defines the term "nonforfeitable" for purposes of these requirements. For purposes of section 411 and the regulations thereunder, a right to an accrued benefit is considered to be nonforfeitable at a particular time if, at that time and thereafter, it is an unconditional right. **Except as provided by paragraph (b) of this section, a right which, at a particular time, is conditioned under the plan upon a subsequent event, subsequent performance, or subsequent forbearance which will cause the loss of such right is a forfeitable right at that time.**

* * *

(b) [Reserved]

* * *

(emphasis added)

26 C.F.R. §1.411(a)-7(a)

§ 1.411(a)-7 Definitions and special rules.

(a) Accrued benefit. For purposes of section 411 and the regulations thereunder, the term "accrued benefit" means–

(1) Defined benefit plan. In the case of a defined benefit plan–

(i) If the plan provides an accrued benefit in the form of an annual benefit commencing at normal retirement age, such

accrued benefit, or

(ii) If the plan does not provide an accrued benefit in the form described in subdivision (i) of this subparagraph, an annual benefit commencing at normal retirement age which is the actuarial equivalent (determined under section 411(c)(3) and §1.411(c)-5) of the accrued benefit determined under the plan. In general, the term "accrued benefits" refers only to pension or retirement benefits. . . .

* * *

26 C.F.R. §1.411(a)-11(d)
(1988 to present)

(d) Distribution valuation requirements. In determining the present value of any distribution of any accrued benefit from a defined benefit plan, the plan must take into account specified valuation rules. For this purpose, the valuation rules are the same valuation rules for valuing distributions as set forth in [Code] section 417(e); see §1.417(e)-1(d) . . . **This paragraph also applies whether or not the participant's consent is required under paragraphs (b) and (c) of this section.**

(emphasis added)

26 C.F.R. §1.417(e)-1T
(temporary regulation, 1985 to 1988)

(a) Scope -- (1) New requirements. Section 417(e) restricts the ability of certain qualified plans to distribute any portion of a participant's accrued benefits without the consent of the participant and the participant's spouse. It also requires the present value of accrued benefits to be calculated using specified interest rates. . . . A plan does not satisfy the requirements of sections 401(a)(11) and 417 unless it satisfies the consent requirements, the determination of present value requirements and the other requirements set forth in this

section. . . .

(b) Consent, etc. requirements . . .

(2) Consent. (i) Written consent of the participant and, if the participant is married at the time of the commencement of the distribution of benefits, the participant's spouse (or, if either the participant or the spouse has died, the survivor) is required before the commencement of the distribution of any part of an accrued benefit if the present value of the nonforfeitable accrued benefit is greater than $3,500. . . .

(ii) In determining the present value of the nonforfeitable accrued benefit, a defined benefit plan must use an interest rate not greater than the rate used by the Pension Benefit Guaranty Corporation (PBGC) to value immediate annuities for plans terminating as of either (A) the proposed distribution (or benefit commencement) date or (B) the first day of the plan year that contains the proposed distribution (or benefit commencement) date (the PBGC rate.).

* * *

(e) Present value requirement -- (1) Interest rate. For purposes of determining the present value of any accrued benefit and for purposes of determining the amount (subject to section 415) of any distribution, a defined benefit plan must use an interest rate not greater than the PBGC rate determined in the same manner and time as set forth in paragraph (b)(2)(ii). The same rate must be used for both purposes.

* * *

26 C.F.R. §1.417(e)-1(d)
(as formulated from 1988 to 1995)

(d) Present value requirement--(1) Requirements. For purposes of determining the present value of any accrued benefit and for purposes of determining the amount . . . of any distribution including a single sum, a defined benefit plan is subject to the interest rate limitations described in subparagraph (2) of this paragraph (d) . . . **The present value of any optional form of benefit cannot be less than the present value of the normal retirement benefit determined in accordance with this paragraph.**

(2) Section 417 interest rate. The [Code] section 417 interest rate is (i) the rate or rates that would be used by the Pension Benefit Guaranty Corporation (PBGC) for a trusteed single-employer plan to value the participant's (or beneficiary's) vested benefit ("applicable interest rate") if the present value of such benefit does not exceed $25,000 and (ii) 120 percent of the applicable interest, as determined in accordance with (i) above, if such present value exceeds $25,000. In no event shall the present value determined by use of 120 percent of the applicable interest rate result in a present value less than $25,000. . . . The applicable interest rates are the interest rates that would be used (as of the date of the distribution) by the PBGC for purposes of determining the present value of that benefit upon termination of an insufficient trustee single-employer plan. Except as otherwise provided by the Commissioner, the applicable interest rates are determined by PBGC regulations. See 29 CFR part 2619 for the applicable PBGC rates.

* * *

(emphasis added)

26 C.F.R. §1.417(e)-1(d)
(as formulated from 1995 to present)

(d) Present value requirement -- (1) General rule. A defined benefit plan must provide that the present value of any accrued benefit and the amount (subject to sections 411(c)(3) and 415) of any distribution, including a single sum, must not be less than the amount calculated using the applicable interest rate described in paragraph (d)(3) of this section (determined for the month described in paragraph (d)(4) of this section) and the applicable mortality table described in paragraph (d)(2) of this section. The present value of any optional form of benefit cannot be less than the present value of the normal retirement benefit determined in accordance with the preceding sentence. The same rules used for the plan under this paragraph (d) must also be used to compute the present value of the benefit for purposes of determining whether consent for a distribution is required under paragraph (b) of this section.

(2) Applicable mortality table. The applicable mortality table is the mortality table based on the prevailing commissioners' standard table (described in section 807(d)(5)(A)) used to determine reserves for group annuity contracts issued on the date as of which present value is being determined (without regard to any other subparagraph of section 807(d)(5)), that is prescribed by the Commissioner in revenue rulings, notices, or other guidance published in the Internal Revenue Bulletin (see @ 601.601(d)(2)(ii)(b) of this chapter). The Commissioner may prescribe rules that apply in the case of a change to the prevailing commissioners' standard table (described in section 807(d)(5)(A)) used to determine reserves for group annuity contracts, in revenue rulings, notices, or other guidance published in the Internal Revenue Bulletin (see § 601.601(d)(2)(ii)(b) of this chapter).

(3) Applicable interest rate -- (i) General rule. The applicable interest rate for a month is the annual interest rate on 30-year Treasury securities as specified by the Commissioner for that month in revenue rulings, notices or other guidance published in the Internal Revenue Bulletin (see § 601.601(d)(2)(ii)(b) of this chapter).

* * *

[Note: The foregoing provisions were initially set forth in temporary TR 1.417(e)-1T, and incorporated by reference in TR 1.417(e)-1(d) (1995-present)].

26 C.F.R. §601.201

§ 601.201 Rulings and determinations letters.

(a) General practice and definitions. (1) It is the practice of the Internal Revenue Service to answer inquiries of individuals and organizations, whenever appropriate in the interest of sound tax administration, **as to their status for tax purposes and as to the tax effects of their acts or transactions.** One of the functions of the National Office of the Internal Revenue Service is to issue rulings in such matters. . . . District directors apply the statutes, regulations, Revenue Rulings, and other precedents published in the Internal Revenue Bulletin in the determination of tax liability, the collection of taxes, and the issuance of determination letters in answer to taxpayers' inquiries or requests. For purposes of this section any reference to district director or district office also includes, where appropriate, the Office of the Director, Office of International Operations.

(2) A "ruling" is a written statement issued to a taxpayer or his authorized representative by the National Office which interprets and applies the tax laws to a specific set of facts. Rulings are issued only by the National Office. The issuance of rulings is under the general supervision of the Assistant

Commissioner (Technical) and has been largely redelegated to the Director, Corporation Tax Division and Director, Individual Tax Division.

(3) A "determination letter" is a written statement issued by a district director in response to a written inquiry by an individual or an organization that applies to the particular facts involved, the principles and precedents previously announced by the National Office. A determination letter is issued only where a determination can be made on the basis of clearly established rules as set forth in the statute, Treasury decision, or regulation, or by a ruling, opinion, or court decision published in the Internal Revenue Bulletin. Where such a determination cannot be made, such as where the question presented involves a novel issue or the matter is excluded from the jurisdiction of a district director by the provisions of paragraph (c) of this section, a determination letter will not be issued. However, **with respect to determination letters in the pension trust area, see paragraph (o) of this section.**

* * *

(l) Effect of rulings. (1) A taxpayer may not rely on an advance ruling issued to another taxpayer. **A ruling, except to the extent incorporated in a closing agreement, may be revoked or modified at any time in the wise administration of the taxing statutes.** . . . If a ruling is revoked or modified, the revocation or modification applies to all open years under the statutes, unless the Commissioner or his delegate exercises the discretionary authority under section 7805(b) of the Code to limit the retroactive effect of the revocation or modification. The manner in which the Commissioner or his delegate generally will exercise this authority is set forth in this section. . . .

* * *

(4) **A ruling found to be in error or not in accord with the current views of the Service may be modified or revoked.** Modification or revocation may be effected by a notice to the taxpayer to whom the ruling originally was issued, or by a Revenue Ruling or other statement published in the Internal Revenue Bulletin.

(5) Except in rare or unusual circumstances, the revocation or modification of a ruling will not be applied retroactively with respect to the taxpayer to whom the ruling was originally issued **or to a taxpayer whose tax liability was directly involved in such ruling** if (i) there has been no misstatement or omission of material facts, (ii) the facts subsequently developed are not materially different from the facts on which the ruling was based, (iii) there has been no change in the applicable law, (iv) the ruling was originally issued with respect to a prospective or proposed transaction, and (v) the taxpayer directly involved in the ruling acted in good faith in reliance upon the ruling and the retroactive revocation would be to his detriment. **To illustrate, the tax liability of each employee covered by a ruling relating to a pension plan of an employer is directly involved in such ruling.** . . .

(m) Effect of determination letters. A determination letter issued by a district director in accordance with this section will be given the same effect upon examination of the return of the taxpayer to whom the determination letter was issued as is described in paragraph (l) ["L"] of this section, in the case of a ruling issued to a taxpayer, except that reference to the National Office is not necessary where, upon examination of the return, it is the opinion of the district director that a conclusion contrary to that expressed in the determination letter is indicated. A district director may not limit the modification or revocation of a determination letter but may refer the matter to the National Office for exercise by the Commissioner or his delegate of the authority to limit the modification or revocation. In this connection see also paragraphs (n) and (o) of this section.

* * *

(o) **Employees' trusts or plans -- (1) In general. Paragraph (o) provides procedures relating to the issuance of determination letters with respect to the qualification of retirement plans.** Paragraph (o)(2) of this section sets forth the authority of key district directors to issue determination letters. . .

(2) Determination letters. (i) **The district directors of the key district offices (described in paragraph (o)(4) of this section) shall have the authority to issue determination letters involving the provisions of sections 401, 403 (a), 405, and 501(a) of the Internal Revenue Code of 1954** with respect to:

(a) Initial qualification of stock bonus, pension, profit-sharing, annuity, and bond purchase plans;

(b) Initial exemption from Federal income tax under section 501(a) of trusts forming a part of such plans . . .

* * *

(ii) **Determination letters authorized by paragraph (o)(2)(i) of this section do not include determinations or opinions relating to other inquiries with respect to plans or trusts. Thus, except as specifically provided in paragraph (o)(2)(i) of this section, key district directors may not issue determination letters relating to issues under other sections of the Code, such as sections 72, 402 through 404, 412, 502, 503, and 511 through 515** . . .

* * *

(emphasis added).

OTHER TREASURY/IRS AUTHORITY

IRS Publication 794

FAVORABLE DETERMINATION LETTER
(Rev. April 1, 1994)
Catalog Number 20630M

INTRODUCTION

This publication explains the significance of your favorable determination letter, points out some features that may affect the qualified status of your employee retirement plan and nullify your determination letter without specific notice from us, and provides general information on the reporting requirements for your plan.

SIGNIFICANCE OF A FAVORABLE DETERMINATION LETTER

An employee retirement plan qualified under Internal Revenue Code section 401(a) (qualified plan) is entitled to favorable tax treatment. For example, contributions made in accordance with the plan document are generally currently deductible. However, participants will not include these contributions into income until the time they receive a distribution from the plan, at which time special income averaging rates for lump sum distributions may serve to reduce the tax liability. In some cases, taxation may be further deferred by rollover to another qualified plan or individual retirement arrangement. (See Publication 575, Pension and Annuity Income, for further details.) Finally, plan earnings may accumulate free of tax.

Employee retirement plans that fail to satisfy the requirements under Code section 401(a) are not entitled to favorable tax treatment. Therefore, many employers desire advance assurance that the terms of their plans satisfy the qualification

requirements. The Internal Revenue Service provides such advance assurance by means of the determination letter program. A favorable determination letter indicates that, in the opinion of the Service, the terms of the plan conform to the requirements of Internal Revenue Code section 401(a). In addition, a favorable determination letter may indicate that, on the basis of other information provided in your application, it has been demonstrated that the plan satisfies certain nondiscrimination requirements of Code section 401(a). See the following topic, Limitations of a Favorable Determination Letter, for more details.

LIMITATIONS OF A FAVORABLE DETERMINATION LETTER

A favorable determination letter is limited in scope and may also have a limited useful life. A determination letter generally applies to qualification requirements regarding the form of the plan. A determination letter may also apply to other qualification requirements pertaining to the prohibition against discrimination in favor of highly compensated employees. These requirements are generally referred to as the coverage and nondiscrimination requirements. They include the nondiscrimination requirements of section 401(a)(4) of the Code, the minimum coverage requirements of section 410(b), and certain related requirements.

The extent to which a determination letter applies to the coverage and nondiscrimination requirements depends on the terms of the plan, the scope of the determination you requested, and the additional information you supplied with your application. Your determination letter will contain specific statements that will describe the scope of reliance represented by the letter.

In addition, the following apply generally to all determination letters:

* The determination letter may not include a statement regarding the minimum coverage requirements of Code section 410(b); this means that you have demonstrated that the plan satisfies these requirements by satisfying the ratio-percentage test.

* A favorable determination letter means that you have demonstrated that the plan satisfies the minimum participation requirements of Code section 401(a)(26). (Letters for certain governmental plans may also include a statement regarding a special effective date rule.)

* If you maintain two or more retirement plans some of which were either not submitted to the Service for determination or not disclosed on each application, certain limitations and requirements will not have been considered on an aggregate basis. Therefore, you may not rely on the determination letter regarding the plans when considered as a total package.

* A determination letter does not consider the special requirements relating to affiliated service groups or leased employees unless the letter includes a statement that the requirements of Internal Revenue Code section 414(m) (affiliated service groups), or 414(n) (leased employees) have been considered.

* For plans that are not amended to comply with the final nondiscrimination regulations retroactively to the 1989 plan year, a determination letter may not be relied upon as to whether plan provisions satisfy a good faith interpretation of the requirements of section 401(a)(4) and related sections of the Code.

* No determination letter may be relied on with respect

to the effective availability of benefits, rights, or features under the plan. (See section 1.401(a)(4)-4(c) of the Income Tax Regulations.) Reliance on whether benefits, rights, or features are currently available to a nondiscriminatory group of employees is provided to the extent specified in the letter.

* A determination letter does not consider whether actuarial assumptions are reasonable for funding or deduction purposes or whether a specific contribution is deductible.

* A determination letter does not consider and may not be relied on with respect to certain other matters described in section 4.08 of Rev. Proc. 93-39, 1993-31 I.R.B. 7 (i.e., whether a plan amendment is part of a pattern of amendments that significantly discriminates in favor of highly compensated employees; the use of the substantiation guidelines contained in Rev. Proc. 93-42, 1993-31 I.R.B. 32; and certain qualified separate lines of business requirements of section 414(r) of the Code).

* The determination letter applies only to the employer and its participants on whose behalf the determination letter was issued.

Become familiar with the terms of the determination letter. Please call the contact person listed on the determination letter if you do not understand any terms in your determination letter.

Retention of information. Whether a plan qualifies is determined from the information in the written plan document and the supporting information submitted by the employer. Therefore, you must retain copies of any demonstrations or other information submitted with your application. Such demonstrations determine the extent of reliance provided by your determination letter. Failure to retain such information may limit the scope of reliance on issues for which demonstrations were provided. **The**

determination letter will not provide reliance if:

(1) there has been a misstatement or omission of material facts,

(2) the facts subsequently developed are materially different than the facts on which the determination was made, or

(3) there is a change in applicable law.

Law changes affecting the plan. In general, a determination letter is issued based on the law in effect at the time the application is received. However, your letter may include a statement indicating any exception to this rule.

Amendments to the plan. A favorable determination letter may no longer apply if there is a change in a statute, regulation, or revenue ruling applicable to the qualification of the plan. However, the determination letter will continue to apply for years before the effective date of the statute, regulation, or revenue ruling. If the letter no longer applies to the plan, the plan must be amended to comply with the new requirements to maintain its qualified status.

* * *

PLAN MUST QUALIFY IN OPERATION

Generally, a plan qualifies in operation if it continues to satisfy the coverage and non-discrimination requirements and is maintained according to the terms on which the favorable determination letter was issued. Changes in facts and other bases on which the determination letter was issued may mean that the determination letter may no longer be relied upon.

Some examples of the effect of a plan's operation on a favorable determination are:

Not meeting nondiscrimination in amount requirement. If the determination letter states that the plan satisfies the nondiscrimination in amount requirement of section 1.401(a)(4)-1(b)(2) of the regulations on the basis of a design-based safe harbor, the plan will generally continue to satisfy this requirement in operation if the plan is maintained according to its terms. If the determination letter states that the plan satisfies the nondiscrimination in amount requirement on the basis of a nondesign-based safe harbor or a general test, and the plan subsequently fails to meet this requirement in operation, the letter may no longer be relied upon with respect to this requirement.

Not meeting minimum coverage requirements. If the determination letter does not include a statement regarding the minimum coverage requirements of Code section 410(b), this means that the plan satisfies these requirements by satisfying the ratio-percentage test. However, if the plan subsequently fails to satisfy the ratio- percentage test in operation, the letter may no longer be relied upon with respect to the coverage requirements. Likewise, if the determination letter states the plan satisfies the average benefit test, the letter may no longer be relied on with respect to the coverage requirements once the plan fails to satisfy the average benefit test in operation.

Changes in testing methods. If the determination letter is based in part on a demonstration that a coverage or nondiscrimination requirement is satisfied, and, in the operation of the plan, the method used to test that this requirement continues to be satisfied is changed (or is required to be changed because the facts have changed) from the method employed in the demonstration, the letter may no longer be relied upon with respect to this requirement.

* * *

(emphasis added in text, only, not headings).

A-47

IRS Notice 96-8

Internal Revenue Service (I.R.S.)

Notice

CASH BALANCE PENSION PLANS

Released: January 18, 1996

Published: February 5, 1996

Determining amount of single sum distributions from cash balance plans. This notice provides guidance concerning the requirements of section 411(a) and 417(e) with respect to the determination of the amount of a single sum distribution from a cash balance plan. The notice also describes proposed guidance to be issued later in regulations that would provide a list of standard indices and associated margins for use by cash balance plans in determining the amount of interest credits.

I. Purpose

This notice describes and requests comments on proposed guidance concerning the application of sections 411 and 417(e) to single sum distributions under defined benefit pension plans that are cash balance plans. The proposed guidance is being described in this notice in order to permit advance public comment in anticipation of the publication of regulations that incorporate the proposed guidance.

II. Background

A. General description of cash balance plans

In general terms, a cash balance plan is a defined benefit pension plan that defines benefits for each employee by

reference to the amount of the employee's hypothetical account balance. An employee's hypothetical account balance is credited with hypothetical allocations and hypothetical earnings determined under a formula selected by the employer and set forth in the plan. These hypothetical allocations and hypothetical earnings are designed to mimic the allocations of actual contributions and actual earnings to an employee's account that would occur under a defined contribution plan. Cash balance plans often specify that hypothetical earnings (referred to in this notice as interest credits) are determined using an interest rate or rate of return under a variable outside index (e.g., the annual yield on one-year Treasury securities). Most cash balance plans also are designed to permit, after termination of employment, a distribution of an employee's entire accrued benefit in the form of a single sum distribution equal to the employee's hypothetical account balance as of the date of the distribution. Many cash balance plans also provide that if distribution is in the form of an annuity, the amount of the annuity is determined by dividing the hypothetical account balance by an annuity conversion factor.

As explained below, in order to comply with sections 411(a) and 417(e) in calculating the amount of a single sum distribution under a cash balance plan, the balance of the employee's hypothetical account must be projected to normal retirement age and then the employee must be paid at least the present value, determined in accordance with section 417(e), of that projected hypothetical account balance. If a cash balance plan provides interest credits using an interest rate that is higher than the section 417(e) applicable interest rate, payment of a single sum distribution equal to the hypothetical account balance as a complete distribution of the employee's accrued benefit may result either in a violation of section 417(e) or a forfeiture in violation of section 411(a). This is because, in such a case, the present value of the employee's accrued benefit, determined using the section 417(e) applicable interest rate, will generally exceed the hypothetical account balance. The

following example illustrates this potential problem.

Example. A cash balance plan provides for interest credits at a fixed rate of 8% per annum that are not conditioned on continued employment, and for annuity conversions using the section 417(e) applicable interest rate and mortality table. A fully vested employee with a hypothetical account balance of $45,000 terminates employment at age 45 and elects an immediate single sum distribution. At the time of the employee's termination, the section 417(e) applicable interest rate is 6.5%.

The projected balance of the employee's hypothetical account as of normal retirement age is $209,743. If $209,743 is discounted to age 45 at 6.5% (the section 417(e) applicable interest rate), the present value equals $59,524.

Accordingly, if the plan paid the hypothetical account balance of $45,000, instead of $59,524, the employee would receive $14,524 less than the amount to which the employee is entitled.

Even if a cash balance plan provides interest credits using an interest rate that exceeds the section 417(e) applicable interest rate, the plan can satisfy sections 417(e) and 411(a). Such a plan would provide that the amount of any single sum distribution is equal to the present value of the employee's accrued benefit determined in a manner that satisfies sections 411(a) and 417(e) even if the amount of the single sum exceeds the employee's hypothetical account balance. Thus, in the example above, the plan would satisfy sections 411(a) and 417(e) if the employee received a single sum distribution of $59,524 (the present value of the employee's accrued benefit) rather than $45,000 (the employee's hypothetical account balance).

B. Existing regulatory safe harbor for cash balance plans

Section 1.401(a)(4)-8(c) of the Income Tax Regulations, as issued in September 1991, provides a safe harbor testing method for cash balance plans. Under this method, a cash

balance plan could be tested for nondiscrimination as though it were a defined contribution plan with actual allocations equal to the amount of the hypothetical allocations credited for the plan year. In order to use the safe harbor, a cash balance plan must satisfy certain design requirements that relate to the accrued benefit and valuation rules that are unique to defined benefit plans.

Comments on the September 1991 regulations expressed concern that the safe harbor plan design requirements reflected an interpretation by the Service and Treasury of the qualification requirements that, in certain cases, would require cash balance plans to pay a single sum distribution in excess of the hypothetical account balance. Guidance was requested on the circumstances in which a cash balance plan (whether or not it qualifies for safe harbor nondiscrimination testing) is permitted to distribute a single sum distribution equal to the hypothetical account balance without violating section 411(a) or 417(e).

When revised regulations under section 401(a)(4) were issued in September 1993, the safe harbor testing method for cash balance plans was left unchanged. The Preamble to those regulations indicated that the safe harbor testing method for cash balance plans had generated significant comment and that further guidance would be issued at a later date.

III. Analysis

A. Nonforfeiture and accrual rules

A cash balance plan is a defined benefit plan, not a defined contribution plan, because the benefits provided are not based solely on actual contributions and forfeitures allocated to an employee's account and the actual investment experience and expenses of the plan allocated to the account. Section 411(a)(7) defines an employee's accrued benefit differently for defined benefit plans than for defined contribution plans. Also, defined benefit plans are subject to a number of statutory

provisions that do not apply to defined contribution plans. These include the rules of section 411(b)(1) that limit "backloading" of accruals; the valuation rules of section 417(e); and the definitely determinable benefits requirement of section 401(a)(25). These provisions limit the extent to which a cash balance plan can mimic the benefit and accrual structure of a defined contribution plan.

Under section 411(a)(2), an employee's accrued benefit must become nonforfeitable in accordance with one of the schedules specified in that section. Under s 1.411(a)-7(a)(1)(ii), the term "accrued benefits" generally refers only to pension or retirement benefits. Under section 411(b)(1), the accrual of the retirement benefits payable at normal retirement age must satisfy one of the rules in section 411(b)(1)(A), (B) or (C).

Under a cash balance plan, the retirement benefits payable at normal retirement age are determined by reference to the hypothetical account balance as of normal retirement age, including benefits attributable to interest credits to that age. Thus, benefits attributable to interest credits must be taken into account in determining whether the accrual of the retirement benefits under a cash balance plan satisfies one of the rules in section 411(b)(1)(A), (B) or (C). **Moreover, benefits attributable to interest credits are in the nature of accrued benefits within the meaning of s 1.411(a)-7(a), rather than ancillary benefits, and thus, once accrued, must become nonforfeitable in accordance with a vesting schedule that satisfies section 411(a).**

Cash balance plans can be categorized based on when the benefits attributable to interest credits accrue. **Under one type of cash balance plan (referred to in this notice as a frontloaded interest credit plan), future interest credits to an employee's hypothetical account balance are not conditioned upon future service.** (Of course, benefits attributable to future interest credits may be forfeited in accordance with the plan's vesting provisions, to the extent permitted under section 411.) **Thus, in the case of a frontloaded interest credit plan, the benefits attributable to future interest credits with respect to a hypothetical allocation accrue at the same time that the**

benefits attributable to the hypothetical allocation accrue. As a result, if an employee terminates employment and defers distribution to a later date, interest credits will continue to be credited to that employee's hypothetical account.

A second type of cash balance plan (referred to in this notice as a backloaded interest credit plan) conditions future interest credits upon further service. **In the case of a backloaded interest credit plan, benefits attributable to interest credits do not accrue until the interest credits are credited to the employee's account. Because backloaded interest credit plans typically will not satisfy any of the accrual rules in section 411(b)(1)(A), (B) or (C), it is anticipated that the proposed guidance will address only frontloaded interest credit plans.**

B. Single sum distributions from **frontloaded** interest credit plans

As indicated above, most cash balance plans are designed to permit a distribution of an employee's entire accrued benefit, after termination of employment, in the form of a single sum equal to the employee's hypothetical account balance as of the date of the distribution. In order for a defined benefit plan to satisfy section 417(e), any single sum distribution payable to an employee from the plan must not be less than the nonforfeitable portion of the present value of the employee's accrued benefit under section 411(a)(7) (determined using the applicable interest rate and mortality table under section 417(e)).

1. Determination of the accrued benefit

In the case of a frontloaded interest credit plan, an employee's accrued benefit as of any date before attainment of normal retirement age is based on the employee's hypothetical account balance as of normal retirement age, including future interest credits to that age. If such a plan

specifies a fixed interest rate for use in determining future interest credits, the employee's hypothetical account balance as of normal retirement age (including future interest credits) can be calculated precisely before normal retirement age. However, if a frontloaded interest credit plan specifies a variable outside index for use in determining the amount of interest credits, the precise dollar amount of an employee's hypothetical account balance as of normal retirement age (including future interest credits to normal retirement age), and thus the precise dollar amount of the employee's accrued benefit as of any date before normal retirement age, cannot be calculated prior to normal retirement age.

A frontloaded interest credit plan that specifies a variable outside index for use in determining the amount of interest credits must prescribe the method for reflecting future interest credits in the calculation of an employee's accrued benefit. In order to comply with section 401(a)(25), the method, including actuarial assumptions, if applicable, must preclude employer discretion. Further, in determining the amount of an employee's accrued benefit, a forfeiture, within the meaning of s 1.411(a)-4T, will result if the value of future interest credits is projected using a rate that understates the value of those credits or if the plan by its terms reduces the interest rate or rate of return used for projecting future interest credits. **A forfeiture in violation of section 411(a) also will occur if, in determining the amount of an employee's accrued benefit, future interest credits are not taken into account (i.e., there is no projection of future interest credits) and this has the same effect as using a rate that understates the value of future interest credits.**

2. Calculation of the present value of the employee's accrued benefit

In the case of a frontloaded interest credit plan, a single sum distribution optional form of benefit equal to the hypothetical account balance will satisfy section 417(e) only if the single sum distribution is not less than the present value of the

employee's accrued benefit calculated in accordance with the applicable interest rate and mortality table under section 417(e)(3). As noted above, the amount of the employee's accrued benefit must be determined using a method of reflecting future interest credits that satisfies section 401(a)(25) and that does not create a forfeiture in violation of section 411(a).

3. Situations in which the present value will not exceed the hypothetical account balance

A frontloaded interest credit plan might provide that the amount of interest credits is determined using a variable interest rate or rate of return that, by its terms, is no greater than the applicable interest rate under section 417(e)(3). For example, a plan that has been amended to comply with the changes to section 417(e) made by the Retirement Protection Act of 1994 (RPA '94) might provide that interest credits are determined using the lesser of the current rate of interest on 30-year Treasury securities or the current yield on 1-year Treasury Constant Maturities. Under such a plan, future interest credits can, without violating section 411(a), be projected to normal retirement age using a rate that is no greater than the applicable interest rate under section 417(e)(3). In that case, assuming that the annuity conversion factor under the plan is not less than the annuity conversion factor determined using the applicable interest rate and mortality table under section 417(e)(3), the employee's hypothetical account balance will equal or exceed the present value of the employee's accrued benefit determined in accordance with section 417(e). Thus, a single sum distribution equal to the employee's hypothetical account balance under such a plan will satisfy sections 411(a) and 417(e).

In other cases, a single sum distribution equal to an employee's hypothetical account balance will satisfy sections 417(e) and 411(a) if (a) the annuity conversion factor is not less than the annuity conversion factor determined using the

applicable interest rate and mortality table under section 417(e)(3), (b) under the method for reflecting future interest credits in the calculation of an employee's accrued benefit, the future interest credits are projected using a rate that is no greater that the applicable interest rate under section 417(e)(3), and (c) this projection does not result in a forfeiture in violation of section 411(a).

By contrast, **if the interest rate or rate of return under the plan used in determining the amount of interest credits is high relative to the section 417(e)(3) interest rate, the plan cannot distribute a single sum equal to the employee's hypothetical account balance and satisfy sections 411(a) and 417(e).** If such a plan provided that, in determining an employee's accrued benefit, the rate used for projecting the amount of future interest credits was no greater than the interest rate under section 417(e)(3), the projection would result in a forfeiture. Alternatively, if the plan provided for interest credits to be projected using a rate that exceeded the section 417(e) interest rate but then provided for the benefit to be discounted using that same higher rate, the plan would violate section 417(e).

C. Effect of defining the accrued benefit as the hypothetical account balance

The requirements referred to in this notice apply even in the case of a cash balance plan that defines an employee's accrued benefit as an amount equal to the employee's hypothetical account balance. Section 411(a)(7) defines the accrued benefit in terms of benefits payable under the plan at normal retirement age. In a cash balance plan, for an employee who has not attained normal retirement age, whether the employee's retirement benefit payable at normal retirement age under the plan includes benefits attributable to future interest credits depends on whether those benefits have accrued.

If benefits attributable to future interest credits have accrued, and those benefits are disregarded when benefits

commence before normal retirement age, the plan has effectively conditioned entitlement to the benefits attributable to those future interest credits on the employee not taking a distribution prior to normal retirement age. Pursuant to s 1.411(a)-4T, a right that is conditioned under the plan on a subsequent forbearance is a forfeitable right. Accordingly, conditioning entitlement to benefits on the employee not taking a distribution violates the nonforfeitability requirements of section 411(a).

Alternatively, if the benefits attributable to future interest credits have not accrued and will accrue only as of the later dates when the interest credits are included in the hypothetical account balance, the timing of those later accruals must be taken into account in applying the accrual rules of section 411(b)(1). As a result, such a plan typically will not satisfy those accrual rules.

IV. Description of proposal

A. Variable interest rates that may be assumed for these purposes to be no greater than the 30-year Treasury interest rate

It is anticipated that the regulations will set forth a list of standard indices and associated margins for use with frontloaded interest credit plans that provide interest credits equal to the product of the balance of the hypothetical account and the current value of a variable index. (It is anticipated that this proposal will apply without regard to how frequently the rate used to determine interest credits is compounded.) Under a frontloaded interest credit plan that, for this purpose, specifies a variable index equal to the PBGC immediate rate or the sum of one of the standard indices and a margin not greater than the specified margin associated with that standard index, no impermissible forfeiture would result from projecting that the rate used to determine future interest credits for an employee is no greater than the applicable interest rate under section 417(e)(3), as amended by RPA '94.

Thus, if such a plan has been amended to comply with the changes to section 417(e) made by RPA '94, the employee's entire accrued benefit could be distributed in the form of a single sum distribution equal to the employee's hypothetical account balance without violating section 411(a) or 417(e), provided that the plan provides the appropriate annuity conversion factors.

The table below provides the proposed list of standard indices and associated margins. The discount rates on Treasury bills and the yields on Treasury Constant Maturities are the rates reported in the Federal Reserve Bulletin, and the Consumer Price Index is CPI-U, as reported by the Department of Labor. Authority would be delegated to the Commissioner to approve other indices and associated margins.

Standard Index	Associated Margin
The discount rate on 3-month Treasury Bills	175 basis points
The discount rate on 6-month Treasury Bills or 12-month Treasury Bills	150 basis points
The yield on 1-year Treasury Constant Maturities	100 basis points
The yield on 2-year Treasury Constant Maturities or 3-year Treasury Constant Maturities	50 basis points
The yield on 5-year Treasury Constant Maturities or 7-year Treasury Constant Maturities	25 basis points

The yield on 10-year Treasury Constant Maturities or any longer period Treasury Constant Maturities	0 basis points
Annual rate of change of the Consumer Price Index	3 percentage points

In developing these standard indices and associated margins, the Service and Treasury took into account the historical relationship between each of these indices and the rate of interest on 30-year Treasury securities.

Under the proposal, if a frontloaded interest credit plan specified a variable index for use in determining the amount of interest credits that is equal to the sum of a standard index (listed in the table above) and a margin that exceeds the specified margin associated with that standard index, distribution of a single sum equal to the employee's hypothetical account balance would not satisfy both section 411(a) and section 417(e). If such a plan provided that the rate used for projecting the amount of future interest credits was no greater than the interest rate under section 417(e)(3), the projection would result in a forfeiture. Alternatively, if a frontloaded interest credit plan provided for interest credits to be projected using a rate that exceeded the section 417(e) interest rate but then provided for the benefit to be discounted using that same higher rate, the plan would violate section 417(e).

B. Guidance will be prospective

The anticipated regulations will be effective prospectively. In addition, for plan years beginning before the regulations are effective, a frontloaded interest credit plan would not be **disqualified** for failing to satisfy section 411(a) or 417(e) if the amount of the distribution satisfied those sections based on a reasonable, good-faith interpretation of the applicable provisions of the Code, taking into account pre-existing

guidance. For this purpose, plans that comply with the guidance in this notice are deemed to be applying a reasonable, good faith interpretation.

V. Comments

The Service and Treasury invite comments on the **proposal** described in this notice. Comments are specifically requested on other indices for which guidance may be appropriate and on guidance that would facilitate the transition to use of an approved index (including possible guidance with respect to the application of section 411(d)(6)). **Any suggestion of an index (and associated margin, if any) should include an analysis of the historical relationship between the index and the rate for 30-year Treasury securities.** Comments should be submitted in writing, referencing Notice 96-7, and addressed to--

Associate Chief Counsel
(Employee Benefits and Exempt Organizations)
CC:EBEO
ATTN: Cash Balance Guidance
Room 5214
Internal Revenue Service
1111 Constitution Ave., N.W.
Washington, D.C. 20224

VI. Drafting information

The principal author of this notice is Marjorie Hoffman of the Office of the Associate Chief Counsel (Employee Benefits and Exempt Organizations). For further information, contact Ms. Hoffman at 202-622-6030 (not a toll-free number).

Notice 96-8, 1996-1 C.B. 359, 1996-6 I.R.B. 23, 1996 WL 17901 (IRS NOT) (emphasis added)

A-60

Treasury Decision 8360

RULES and REGULATIONS

DEPARTMENT OF THE TREASURY

Internal Revenue Service

26 CFR Part 1

[T.D. 8360]

RIN 1545-AM95

Nondiscrimination Requirements for Qualified Plans

Thursday, September 19, 1991

AGENCY: Internal Revenue Service, Treasury.

ACTION: **Final regulations.**

SUMMARY: This document contains **final regulations** under section 401(a)(4) of the Internal Revenue Code of 1986. They interpret the section 401(a)(4) requirement that contributions or benefits provided under a tax-qualified retirement plan not discriminate in favor of highly compensated employees. This section and the minimum coverage requirements of section 410(b) form a coordinated nondiscrimination rule that prohibits a tax-qualified retirement plan from being designed or operated to favor highly compensated employees.

These **final regulations** reflect changes made by the Tax Reform Act of 1986 and by the Technical and Miscellaneous Revenue Act of 1988. The regulations provide the guidance necessary to comply with the law and affect sponsors of, and participants in, tax-qualified retirement plans. These **final regulations** are issued in conjunction with other sets of final

regulations under sections 401(a)(17), 401(l), 410(b), and 414(s), and were developed in conjunction with final regulations under section 401(a)(26) that will be published in the near future.

EFFECTIVE DATES: These regulations are effective for plan years beginning after December 31, 1991, and applied to those plan years except as set forth in the transition rules of §1.401(a)(4)-13.

FOR FURTHER INFORMATION CONTACT: The attorney listed below for the particular section at 202-377-9372 (not a toll-free number).

§ 1.401-4 Rebecca Wilson or David Munroe
§ 1.401(a)-4 Rebecca Wilson or David Munroe
§ 1.401(a)(4)-1 Rebecca Wilson or David Munroe
§ 1.401(a)(4)-2 Rebecca Wilson or David Munroe
§ 1.401(a)(4)-3 Marjorie Hoffman or David Munroe
§ 1.401(a)(4)-4 Suzanne Tank or David Munroe
§ 1.401(a)(4)-5 Rebecca Wilson or David Munroe
§ 1.401(a)(4)-6 David Munroe
§ 1.401(a)(4)-7 Patricia McDermott
§ 1.401(a)(4)-8 Marjorie Hoffman or David Munroe
§ 1.401(a)(4)-9 David Munroe
§ 1.401(a)(4)-10 Rebecca Wilson or David Munroe
§ 1.401(a)(4)-11 Rebecca Wilson or David Munroe
§ 1.401(a)(4)-12 Rebecca Wilson or David Munroe
§ 1.401(a)(4)-13 Patricia McDermott or David Munroe
§ 411(d)-4 Patricia McDermott or David Munroe

SUPPLEMENTARY INFORMATION: On May 14, 1990, the Internal Revenue Service published in the Federal Register proposed amendments to the Income Tax Regulations (26 CFR part 1) under section 401(a)(4) of the Internal Revenue Code of 1986 (Code) (55 FR 19897). These regulations were proposed in conjunction with regulations under related Internal Revenue Code sections including sections 401(a)(17),

401(a)(26), 410(b), and 414(s) and amendments to regulations under section 401(l). The May 1990 proposed regulations were supplemented and modified by proposed regulations published in the Federal Register on September 14, 1990 (55 FR 37888), and December 3, 1990 (55 FR 49906).

Written comments were received from the public on the proposed regulations. In addition, a public hearing on the May 14, 1990 regulations was announced on May 14, 1990 (55 FR 19897), and a public hearing on the September 14, 1990, regulations was announced on September 14, 1990 (55 FR 37888). These public hearings were held on September 26, 27, and 28, 1990. After consideration of all of the written comments received and the statements made at the public hearing, the proposed regulations under section 401(a)(4) are adopted as modified by this Treasury Decision.

Summary of Significant Modifications

* * *

The following is a brief summary of the more significant substantive modifications in the **final** regulations.
- **New safe harbors are provided for cash balance plans** and section 412(i) insurance contract plans.

* * *

1. Nondiscrimination in Amount of Contributions or Benefits

Overview

* * *

. . . Finally, optional **safe harbor testing methods for** target benefit plans, **cash balance plans**, and defined benefit plans that are part of a floor-offset arrangement **are provided under the cross-testing rules in § 1.401(a)(4)-8.**

* * *

Cash Balance Plans

Several commentators requested clarification of the treatment of cash balance plans, another hybrid plan design that, unlike target benefit plans, was not addressed in the proposed regulations. **Comments indicated that cash balance plans are becoming increasingly popular. Cash balance plans are defined benefit plans that generally determine benefits by reference to an employee's "cash balance" or hypothetical account in a manner analogous to the allocation of contributions and earnings to an employee's account under a defined contribution plan. Under a cash balance plan, each employee's hypothetical account is the sum of the hypothetical allocations for prior plan years provided under a hypothetical allocation formula resembling the allocation formula under a defined contribution plan, plus subsequent interest adjustments through normal retirement age.**

The final regulations have added a safe harbor testing method for cash balance plans. Because cash balance plans are defined benefit plans that calculate benefits in a manner similar to defined contribution plans, **the safe harbor testing method is provided under the cross-testing rules of § 1.401(a)(4)-8(c). The safe harbor testing method permits a cash balance plan to be tested on the basis of the hypothetical allocation formula used to determine an employee's cash balance, rather than on the actual benefits provided under the plan, if certain conditions are satisfied. Among other requirements, the interest adjustments through normal retirement age must be accrued under the plan in the year the hypothetical allocation to which they relate is accrued,** and interest adjustments must be determined using a fixed interest rate between 7.5 and 8.5 percent, or one of a list of variable interest rates provided in the regulations. The fact that **interest adjustments through normal retirement age are accrued in the year of the related**

hypothetical allocation will not cause a cash balance plan to fail to satisfy the requirements of section 411(b)(1)(H), relating to age-based reductions in the rate at which benefits accrue under a plan. The safe harbor also imposes limitations on the granting of past service credit and the provision of subsidized optional forms of benefit.

Some of the comments involving cash balance plans also requested that the final regulations provide special relief for cash balance plans from the requirements of section 417(e). Section 417(e) prescribes certain interest rates that must be used in determining the amount of a single-sum benefit provided under a defined benefit plan. These rates, when combined into a single blended rate, are sometimes lower than the rates used by existing cash balance plans in determining employees' cash balances, and can therefore require a plan that does not use the section 417(e) rates to determine interest adjustments to pay an employee more than the amount of the employee's hypothetical cash balance when benefits are paid in a single sum. The Treasury and the Service have determined that such relief cannot be granted consistent with the requirements of section 417(e). However, in order to minimize the occasions when this problem will arise, the final regulations include a blended section 417(e) interest rate among the alternative safe harbor interest rates a cash balance plan may use in determining interest adjustments.

* * *

6. Cross-Testing Defined Benefit and Defined Contribution Plans

* * *

. . . **As discussed above, the cross testing rules have been expanded to provide safe harbor testing methods for cash balance plans**, to expand the safe harbor testing methods for

floor offset plans, and to clarify the safe harbor testing methods for target benefit plans.

* * *

§ 1.401(a)(4)-8 Cross-testing.

* * *

(c) Nondiscrimination in amount of contributions under a defined benefit plan . . . **Paragraph (c)(3) of this section provides a safe harbor testing method for cash balance plans.**

* * *

(3) Safe harbor testing method for cash balance plans--(i) General rule. A cash balance plan is a defined benefit plan that defines benefits for each employee by reference to the employee's hypothetical account. An employee's hypothetical account is determined by reference to hypothetical allocations and interest adjustments that are analogous to actual allocations of contributions and earnings to an employee's account under a defined contribution plan. Because a cash balance plan is a defined benefit plan, whether it satisfies section 401(a)(4) with respect to the equivalent amount of contributions is generally determined under paragraphs (c)(1) and (c)(2) of this section. However, **a cash balance plan that satisfies each of the requirements in paragraphs (c)(3)(ii) through (xi) of this section is deemed to satisfy section 401(a)(4) with respect to an equivalent amount of contributions.**

(ii) Plan requirements in general. The plan must be an accumulation plan. The benefit formula under the plan must provide for hypothetical allocations for each employee in the plan that satisfy paragraph (c)(3)(iii) of this section, and interest adjustments to these hypothetical allocations that satisfy paragraph (c)(3)(iv) of this section. The benefit formula

under the plan must provide that these hypothetical allocations and interest adjustments are accumulated as a hypothetical account for each employee, determined in accordance with paragraph (c)(3)(v) of this section. **The plan must provide that an employee's accrued benefit under the plan as of any date is an annuity that is the actuarial equivalent of the employee's projected hypothetical account as of normal retirement age, determined in accordance with paragraph (c)(3)(vi) of this section. In addition, the plan must satisfy paragraphs (c)(3)(vii) through (xi) of this section (to the extent applicable) regarding optional forms of benefit**, past service credits, post-normal retirement age benefits, certain uniformity requirements, and changes in the plan's benefit formula, respectively.

(iii) Hypothetical allocations-- (A) In general. The hypothetical allocations provided under the plan's benefit formula must satisfy either paragraph (c)(3)(iii)(B) or (C) of this section. Paragraph (c)(3)(iii)(B) of this section provides a design-based safe harbor that does not require the annual comparison of hypothetical allocations under the plan. Paragraph (c)(3)(iii)(C) of this section requires the annual comparison of hypothetical allocations.

(B) Uniform hypothetical allocation formula. To satisfy this paragraph (c)(3)(iii)(B), the plan's benefit formula must provide for hypothetical allocations for all employees in the plan for all plan years of amounts that would satisfy § 401(a)(4)-2(b)(3) for each such plan year if the hypothetical allocations were the only allocations under a defined contribution plan for the employees for those plan years. Thus, the plan's benefit formula must provide for hypothetical allocations for all employees in the plan for all plan years that are the same percentage of plan year compensation or the same dollar amount. In determining whether the hypothetical allocations satisfy § 1.401(a)(4)-2(b)(3), the only provisions of § 1.401(a)(4)-2(b)(5) that apply are § 1.401(a)(4)-2(b)(5)(ii) (section 401(l) permitted disparity, (iii) (entry dates), (vi) (certain limits on allocations), and (vii) (dollar allocation per uniform unit of service). Thus, for example, the plan's benefit

formula may take permitted disparity into account in a manner allowed under § 1.401(l)-2 for defined contribution plans.

(C) Modified general test. To satisfy this paragraph (c)(3)(iii)(C), the plan's benefit formula must provide for hypothetical allocations for all employees in the plan for the plan year that would satisfy the general test in § 1.401(a)(4)-2(c) for the plan year, if the hypothetical allocations were the only allocations for the employees taken into account under § 1.401(a)(4)- 2(c)(2)(ii) under a defined contribution plan for the plan year. In determining whether the hypothetical allocations satisfy § 1.401(a)(4)-2(c), the provisions of § 1.401(a)(4)-2(c)(2)(iii) through (v) apply. Thus, for example, permitted disparity may be imputed under § 1.401(a)(4)-2(c)(2)(iv) in accordance with the rules of § 1.401(a)(4)-7(b) applicable to defined contribution plans.

(iv) Interest adjustments to hypothetical allocations--(A) General rule. The plan benefit formula must provide that the dollar amount of the hypothetical allocation for each employee for a plan year is automatically adjusted using an interest rate that satisfies paragraph (c)(3)(iv)(B) of this section, compounded no less frequently than annually, for the period that begins with a date in the plan year and that ends at normal retirement age. This requirement is not satisfied if any portion of the interest adjustments to a hypothetical allocation are contingent on the employee's satisfaction of any requirement. Thus, for example, the interest adjustments to a hypothetical allocation must be provided through normal retirement age, even though the employee terminates employment or commences benefits before that age.

(B) Requirements with respect to interest rates. The interest rate must be a single interest rate specified in the plan that is the same for all employees in the plan for all plan years. The interest rate must be either a standard interest rate or a variable interest rate. If the interest rate is a variable interest rate, it must satisfy paragraph (c)(3)(iv)(C) of this section.

(C) Variable interest rates--(1) General rule. The plan must

specify the variable interest rate, the method for determining the current value of the variable interest rate, and the period (not to exceed 1 year) for which the current value of the variable interest rate applies. Permissible variable interest rates are listed in paragraph (c)(3)(iv)(C)(2) of this section. Permissible methods for determining the current value of the variable interest rate are provided in paragraph (c)(3)(iv)(C)(3) of this section.

(2) Permissible variable interest rates. The variable interest rate specified in the plan must be one of the following--

(i) The rate on 3-month Treasury Bills,

(ii) The rate on 6-month Treasury Bills,

(iii) The rate on 1-year Treasury Bills,

(iv) The yield on 1-year Treasury Constant Maturities,

(v) The yield on 2-year Treasury Constant Maturities,

(vi) The yield on 5-year Treasury Constant Maturities,

(vii) The yield on 10-year Treasury Constant Maturities,

(viii) The yield on 30-year Treasury Constant Maturities, or

(ix) The single interest rate such that, as of a single age specified in the plan, the actuarial present value of a deferred straight life annuity of an amount commencing at the normal retirement age under the plan, calculated using that interest rate and a standard mortality table but assuming no mortality before normal retirement age, is equal to the actuarial present value, as of the single age specified in the plan, of the same annuity calculated using the section 417(e) rates applicable to distributions in excess of $25,000 (determined under § 1.417(e)-1(d)), and the same mortality assumptions.

(3) Current value of variable interest rate. The current value of the variable interest rate that applies for a period must be either the value of the variable interest rate determined as of a specified date in the period or the immediately preceding period, or the average of the values of the variable interest rate as of two or more specified dates during the current period or the immediately preceding period. The value as of a date of the rate on a Treasury Bill is the average auction rate for the week or month in which the date falls, as reported in the Federal Reserve Bulletin. The value as of a date of the yield on

a Treasury Constant Maturity is the average yield for the week, month, or year in which the date falls, as reported in the Federal Reserve Bulletin. (The Federal Reserve Bulletin is published by the Board of Governors of the Federal Reserve System and is available from Publication Services, Mail Stop 138, Board of Governors of the Federal Reserve System, Washington DC 20551.) The plan may limit the current value of the variable interest rate to a maximum (not less than the highest standard interest rate), or a minimum (not more than the lowest standard interest rate), or both.

(v) Hypothetical account--(A) Current value of hypothetical account. As of any date, the current value of an employee's hypothetical account must equal the sum of all hypothetical allocations and the respective interest adjustments to each such hypothetical allocation provided through the date for the employee under the plan's benefit formula (without regard to any interest adjustments provided under the plan's benefit formula for periods after that date).

(B) Value of hypothetical account as of normal retirement age. Under paragraph (c)(3)(vi) of this section, the value of an employee's hypothetical account must be determined as of normal retirement age in order to determine the employee's accrued benefit as of any date at or before normal retirement age. As of any date at or before normal retirement age, the value of an employee's hypothetical account as of normal retirement age must equal the sum of each hypothetical allocation provided through that date for the employee under the plan's benefit formula, plus the interest adjustments provided through normal retirement age on each of those hypothetical allocations for the employee under the plan's benefit formula (without regard to any hypothetical allocations that might be provided after that date under the plan's benefit formula). If the interest rate specified in the plan is a variable interest rate, the plan must specify that the determination in the preceding sentence is made by assuming that the current value of the variable interest rate for all future periods is either the current value of the variable interest rate for the current period or the average

of the current values of the variable interest rate for the current period and one or more periods immediately preceding the current period (not to exceed 5 years in the aggregate).

(vi) Determination of accrued benefit--(A) Definition of accrued benefit. The plan must provide that at any date at or before normal retirement age the accrued benefit (within the meaning of section 411(a)(7)(A)(i)) of each employee in the plan is an annuity commencing at normal retirement age that is the actuarial equivalent of the employee's hypothetical account as of normal retirement age (as determined under paragraph (c)(3)(v)(B) of this section). The separate benefit that each employee accrues for a plan year is an annuity that is the actuarial equivalent of the employee's hypothetical allocation for that plan year, including the automatic adjustments for interest through normal retirement age required under paragraph (c)(3)(iv) of this section.

(B) Normal form of benefit. The annuity specified in paragraph (c)(3)(vi)(A) of this section must provide an annual benefit payable in the same form at the same uniform normal retirement age for all employees in the plan. The annual benefit must be the normal retirement benefit under the plan (within the meaning of section 411(a)(9)) under the plan.

(C) Determination of actuarial equivalence. For purposes of this paragraph (c)(3)(vi) and paragraph (c)(3)(ix) of this section, actuarial equivalence must be determined using a standard mortality table and either a standard interest rate or the interest rate specified in the plan for making interest adjustments to hypothetical allocations. If the interest rate used is the interest rate specified in the plan, and that rate is a variable interest rate, the assumed value of the variable interest rate for all future periods must be the same value that would be assumed for purposes of paragraph (c)(3)(v)(B) of this section. The same actuarial assumptions must be used for all employees in the plan.

(D) Effect of section 415 and 416 requirements. A plan does not fail to satisfy this paragraph (c)(3)(vi) merely because the

accrued benefits under the plan are limited by section 415, or merely because the accrued benefits under the plan are the greater of the accrued benefits otherwise determined under the plan and the minimum benefit described in section 416(c)(1) (regardless of whether the plan is top-heavy).

(vii) Optional forms of benefit--(A) In general. The plan must satisfy the uniform subsidies requirement of § 1.401(a)(4)-3(b)(2)(iv) with respect to all subsidized optional forms of benefit.

(B) Limitation on subsidies. Unless hypothetical allocations are determined under a uniform hypothetical allocation formula that satisfies paragraph (c)(3)(iii)(B) of this section, the actuarial present value of any QJSA provided under the plan must not be greater than the single sum distribution to the employee that would satisfy paragraph (c)(3)(vii)(C) of this section assuming that it was distributed to the employee on the date of commencement of the QJSA.

(C) Distributions subject to section 417(e). Except as otherwise required under section 415(b), **if the plan provides for a distribution alternative that is subject to the interest rate restrictions under section 417(e), the actuarial present value of the benefit paid to an employee under the distribution alternative must equal the nonforfeitable percentage (determined under the plan's vesting schedule) of the greater of the following two amounts--**

(1) The current value of the employee's hypothetical account as of the date the distribution commences, calculated in accordance with paragraph (c)(3)(v)(A) of this section.

(2) The actuarial present value (calculated in accordance with § 1.417(e)- 1(d)) of the employee's accrued benefit.

(D) Determination of actuarial present value. For purposes of this paragraph (c)(3)(vii), actuarial present value must be determined using a reasonable interest rate and mortality table. A standard interest rate and a standard mortality table are considered reasonable for this purpose.

(viii) Past service credit. . . .

(ix) Employees beyond normal retirement age. . . .

(x) Additional uniformity requirements. . . .

(d) Safe harbor testing method for defined benefit plans that are part of a floor-offset arrangement . . .

* * *

(emphasis added).

PUBLIC LAWS

Pub. L. 93-406, 88 Stat. 829 (Sept. 2, 1974)
Employee Retirement Income Security Act of 1974

//29 USC 1054.//

SEC. 204. BENEFIT ACCRUAL REQUIREMENTS

* * *

(d) Notwithstanding section 203(b) (1), for purposes of determining the employee's accrued benefit under the plan, the plan may disregard service performed by the employee with respect to which he has received-

(1) a distribution of the present value of his entire nonforfeitable benefit if such distribution was in an amount (not more than $1,750) permitted under regulation prescribed by the secretary of the treasury, or

(2) a distribution of the present value of his nonforfeitable benefit attributable to such service which he elected to receive.

* * *

SEC. 1012. MINIMUM VESTING STANDARDS.

(a) In general.-Subpart B of Part I of Subchapter D of Chapter 1 is amended by adding after section 410 //ante, p. 898.// the following new section:

"SEC. 411. MINIMUM VESTING STANDARDS.

"(a) General rule.-A trust shall not constitute a qualified trust under section 401(a) unless the plan of which such trust is a part provides that an employee's right to his normal retirement benefit is nonforfeitable upon the attainment of

normal retirement age (as defined in subsection (a) (8)) . . .

* * *

"(7) Accrued benefit.--

"(a) In general.-For purposes of this section, the term 'accrued benefit' means-

"(i) in the case of a defined benefit plan, the employee's accrued benefit determined under the plan and, except as provided in subsection (c) (3), expressed in the form of an annual benefit commencing at normal retirement age, or

"(ii) in the case of a plan which is not a defined benefit plan, the balance of the employee's account.

"(b) Effect of certain distributions.-Notwithstanding paragraph (4), for purposes of determining the employee's accrued benefit under the plan, the plan may disregard service performed by the employee with respect to which he has received-

"(i) a distribution of the present value of his entire nonforfeitable benefit if such distribution was in an amount (not more than $1,750) permitted under regulations prescribed by the secretary or his delegate, or

"(ii) a distribution of the present value of his nonforfeitable benefit attributable to such service which he elected to receive.

* * *

Pub. L. 98-397, 98 Stat. 1426 (Aug. 23, 1984)
Retirement Equity Act of 1984

SEC. 103. REQUIREMENT OF JOINT AND SURVIVOR ANNUITIES AND PRERETIREMENT SURVIVOR ANNUITIES.

(a) GENERAL RULE. -- Section 205 (29 U.S.C. 1055) is amended to read as follows:

"REQUIREMENT OF JOINT AND SURVIVOR ANNUITY

AND PRERETIREMENT SURVIVOR ANNUITY

"SEC. 205. (a) Each pension plan to which this section applies shall provide that --

"(1) in the case of a vested participant who retires under the plan, the accrued benefit payable to such participant shall be provided in the form of a qualified joint and survivor annuity, and

"(2) in the case of a vested participant who dies before the annuity starting date and who has a surviving spouse, a qualified preretirement survivor annuity shall be provided to the surviving spouse of such participant.

"(b) (1) This section shall apply to --

"(A) any defined benefit plan,

* * *

"(d) For purposes of this section, the term "qualified joint and survivor annuity' means an annuity --

"(1) for the life of the participant with a survivor annuity for the life of the spouse which is not less than 50 percent of (and is not greater than 100 percent of) the amount of the annuity which is payable during the joint lives of the participant and the spouse, and

"(2) which is the actuarial equivalent of a single annuity for the life of the participant.

Such term also includes any annuity in a form having the effect of an annuity described in the preceding sentence.

"(e) For purposes of this section --

"(1) Except as provided in paragraph (2), the term "qualified preretirement survivor annuity' means a survivor annuity for the life of the surviving spouse of the participant if --

"(A) the payments to the surviving spouse under such annuity are not less than the amounts which would be payable as a survivor annuity under the qualified joint and survivor annuity under the plan (or the actuarial equivalent thereof) if --

"(i) in the case of a participant who dies after the date on which the participant attained the earliest retirement age, such participant had retired with an immediate qualified joint and survivor annuity on the day before the participant's date of death, or

"(ii) in the case of a participant who dies on or before the date on which the participant would have attained the earliest retirement age, such participant had --

"(I) separated from service on the date of death,

"(II) survived to the earliest retirement age,

"(III) retired with an immediate qualified joint and survivor annuity at the earliest retirement age, and

"(IV) died on the day after the day on which such participant would have attained the earliest retirement age, and

"(B) under the plan, the earliest period for which the surviving spouse may receive a payment under such annuity is not later than the month in which the participant would have attained the earliest retirement age under the plan.

"(2) In the case of any individual account plan or participant described in subparagraph (B) or (C) of subsection (b)(1), the term "qualified preretirement survivor annuity' means an annuity for the life of the surviving spouse the actuarial equivalent of which is not less than 50 percent of the account balance of the participant as of the date of death.

* * *

"(g)(1) A plan may provide that the present value of a qualified joint and survivor annuity or a qualified preretirement survivor annuity will be immediately distributed if such value does not exceed $3,500. No distribution may be made under the preceding sentence after the annuity starting date unless the participant and the spouse of the participant (or where the participant has died, the surviving spouse) consent in writing to such distribution.

"(2) If --

"(A) the present value of the qualified joint and survivor annuity or the qualified preretirement survivor annuity

exceeds $3,500, and
"(B) the participant and the spouse of the participant (or where the participant has died, the surviving spouse) consent in writing to the distribution, the plan may immediately distribute the present value of such
annuity.
"(3) For purposes of paragraphs (1) and (2), the present value of a qualified joint and survivor annuity or a qualified preretirement survivor annuity shall be determined as of the date of the distribution and by using an interest rate not greater than the interest rate which would be used (as of the date of the distribution) by the Pension Benefit Guaranty Corporation for purposes of determining the present value of a lump sum distribution on plan termination.

* * *

"(h) "29 USC 1002' For purposes of this section --
"(1) the term "vested participant' means any participant who has a nonforfeitable right (within the meaning of section 3(19)) to any portion of the accrued benefit derived from employer contributions,
"(2) the term "annuity starting date' means the first day of the first period for which an amount is received as an annuity (whether by reason of retirement or disability), and
"(3) the term "earliest retirement age' means the earliest date on which, under the plan, the participant could elect to receive retirement benefits.

* * *

SEC. 105. RESTRICTIONS ON MANDATORY DISTRIBUTIONS.

(a) GENERAL RULE. -- Section 203 (29 U.S.C. 1053) is amended by adding at the end thereof the following new subsection:
"(e)(1) If the present value of any accrued benefit exceeds

$3,500, such benefit shall not be treated as nonforfeitable if the plan provides that the present value of such benefit could be immediately distributed without the consent of the participant.

"(2) For purposes of paragraph (1), the present value shall be calculated by using an interest rate not greater than the interest rate which would be used (as of the date of the distribution) by the Pension Benefit Guaranty Corporation for purposes of determining the present value of a lump sum distribution on plan termination.'.

(b) CONFORMING AMENDMENT. -- Paragraph (1) of section 204(d) (29 U. S.C. 1054(d)(1)) is amended by striking out "$1,750' and inserting in lieu thereof "$3,500'.

* * *

SEC. 203. REQUIREMENT OF JOINT AND SURVIVOR ANNUITIES AND PRERETIREMENT SURVIVOR ANNUITIES.

* * *

"SEC. 417. "26 USC 417' DEFINITIONS AND SPECIAL RULES FOR PURPOSES OF MINIMUM SURVIVOR ANNUITY REQUIREMENTS

* * *

"(e) RESTRICTIONS ON CASH-OUTS. --

"(1) PLAN MAY REQUIRE DISTRIBUTION IF PRESENT VALUE NOT IN EXCESS OF $3,500. -- A plan may provide that the present value of a qualified joint and survivor annuity or a qualified preretirement survivor annuity will be immediately distributed if such value does not exceed $3,500. No distribution may be made under the preceding sentence after the annuity starting date unless the participant and the spouse of the participant (or where the participant has died, the surviving spouse) consents in writing to such distribution.

"(2) PLAN MAY DISTRIBUTE BENEFIT IN EXCESS OF $3,500 ONLY WITH CONSENT. -- If --

"(A) the present value of the qualified joint and survivor annuity or the qualified preretirement survivor annuity exceeds $3,500, and

"(B) the participant and the spouse of the participant (or where the participant has died, the surviving spouse) consent in writing to the distribution, the plan may immediately distribute the present value of such annuity.

"(3) DETERMINATION OF PRESENT VALUE. -- For purposes of paragraphs (1) and (2), the present value of a qualified joint and survivor annuity or a qualified preretirement survivor annuity shall be determined as of the date of the distribution and by using an interest rate not greater than the interest rate which would be used (as of the date of the distribution) by the Pension Benefit Guaranty Corporation for purposes of determining the present value of a lump sum distribution on plan termination.

* * *

SEC. 205. RESTRICTIONS ON MANDATORY DISTRIBUTIONS.

(a) "26 USC 411' GENERAL RULE. -- Subsection (a) of section 411 (relating to minimum vesting standards) is amended by adding at the end thereof the following new paragraph:

"(11) RESTRICTIONS ON CERTAIN MANDATORY DISTRIBUTIONS. --

"(A) IN GENERAL. -- If the present value of any accrued benefit exceeds $3,500, such benefit shall not be treated as nonforfeitable if the plan provides that the present value of such benefit could be immediately distributed without the consent of the participant.

"(B) DETERMINATION OF PRESENT VALUE. -- For purposes of subparagraph (A), the present value shall be calculated by using an interest rate not greater than the interest rate which would be used (as of the date of the distribution) by the

Pension Benefit Guaranty Corporation for purposes of determining the present value of a lump sum distribution on plan termination.'.

(b) "26 USC 411' CONFORMING AMENDMENT. -- Subparagraph (B) of section 411(a)(7) (relating to effect of certain distributions) is amended by striking out "$1,750' and inserting in lieu thereof "$3,500'.

* * *

Pub. L. 99-514, 100 Stat. 2085 (Oct. 22, 1986)
Tax Reform Act of 1986

* * *

SEC. 1139. INTEREST RATE ASSUMPTIONS.

(a) IN GENERAL. -- Subparagraph (B) of section 411(a)(11) is amended to read as follows:

"(B) DETERMINATION OF PRESENT VALUE. --

"(i) IN GENERAL. -- For purposes of subparagraph (A), the present value shall be calculated --

"(I) by using an interest rate no greater than the applicable interest rate if the vested accrued benefit (using such rate) is not in excess of $25,000, and

"(II) by using an interest rate no greater than 120 percent of the applicable interest rate if the vested accrued benefit exceeds $25,000 (as determined under subclause (I)).

In no event shall the present value determined under subclause (II) be less than $25,000.

"(ii) APPLICABLE INTEREST RATE. -- For purposes of clause (i), the term 'applicable interest rate' means the interest rate which would be used (as of the date of the distribution) by the Pension Benefit Guaranty Corporation for purposes of determining the present value of a lump sum distribution on plan termination."

(b) CONFORMING AMENDMENT. -- Paragraph (3) of section 417(e) (relating to determination of present value) is amended

to read as follows:

"(3) DETERMINATION OF PRESENT VALUE. --

"(A) IN GENERAL. -- For purposes of paragraphs (1) and (2), the present value shall be calculated --

"(i) by using an interest rate no greater than the applicable interest rate if the vested accrued benefit (using such rate) is not in excess of $25,000, and

"(ii) by using an interest rate no greater than 120 percent of the applicable interest rate if the vested accrued benefit exceeds $25,000 (as determined under clause (i)).

In no event shall the present value determined under subclause (II) be less than $25,000.

"(B) APPLICABLE INTEREST RATE. -- For purposes of subparagraph (A), the term 'applicable interest rate' means the interest rate which would be used (as of the date of the distribution) by the Pension Benefit Guaranty Corporation for purposes of determining the present value of a lump sum distribution on plan termination."

(c) AMENDMENTS TO ERISA. -

(1) IN GENERAL. -- Paragraph (2) of section 203(e) of the Employee Retirement Income Security Act of 1974 (29 U.S.C. 1053(e)(2)) is amended to read as follows:

"(2)(A) For purposes of paragraph (1), the present value shall be calculated --

"(i) by using an interest rate no greater than the applicable interest rate if the vested accrued benefit (using such rate) is not in excess of $25,000, and

"(ii) by using an interest rate no greater than 120 percent of the applicable interest rate if the vested accrued benefit exceeds $25,000 (as determined under clause (i)).

In no event shall the present value determined under subclause (II) be less than $25,000.

"(B) APPLICABLE INTEREST RATE. -- For purposes of subparagraph (A), the term 'applicable interest rate' means the interest rate which would be used (as of the date of the distribution) by the Pension Benefit Guaranty Corporation for purposes of determining the present value of a lump sum distribution on plan termination."

(2) CONFORMING AMENDMENT. -- Paragraph (3) of section 205(g) of such Act (29 U.S.C. 1055(g)(3)) is amended to read as follows:

"(3)(A) For purposes of paragraphs (1) and (2), the present value shall be calculated --

"(i) by using an interest rate no greater than the applicable interest rate if the vested accrued benefit (using such rate) is not in excess of $25,000, and

"(ii) by using an interest rate no greater than 120 percent of the applicable interest rate if the vested accrued benefit exceeds $25,000 (as determined under clause (i)).

In no event shall the present value determined under subclause (II) be less than $25,000.

"(B) For purposes of subparagraph (A), the term 'applicable interest rate' means the interest rate which would be used (as of the date of the distribution) by the Pension Benefit Guaranty Corporation for purposes of determining the present value of a lump sum distribution on plan termination.".

Pub. L. 103-465, 108 Stat. 4809 (Dec. 8, 1994)
Retirement Protection Act of 1994

SEC. 767. SINGLE SUM DISTRIBUTIONS.

(a) AMENDMENTS TO INTERNAL REVENUE CODE OF 1986 RELATING TO MINIMUM BENEFITS.--

<< 26 USCA § 411 >>

(1) DETERMINATION OF PRESENT VALUE FOR PURPOSES OF RESTRICTIONS ON MANDATORY DISTRIBUTIONS.--Subparagraph (B) of section 411(a)(11) is amended to read as follows:

"(B) DETERMINATION OF PRESENT VALUE.--For purposes of subparagraph (A), the present value shall be calculated in accordance with section 417(e)(3)."

(2) DETERMINATION OF PRESENT VALUE FOR PURPOSES OF RESTRICTIONS ON CASH-OUTS.--Paragraph (3) of section 417(e) is amended to read as follows:

"(3) DETERMINATION OF PRESENT VALUE.--

"(A) IN GENERAL.--

"(i) PRESENT VALUE.--Except as provided in subparagraph (B), for purposes of paragraphs (1) and (2), the present value shall not be less than the present value calculated by using the applicable mortality table and the applicable interest rate.

"(ii) DEFINITIONS.--For purposes of clause (i)--

"(I) APPLICABLE MORTALITY TABLE.--The term 'applicable mortality table' means the table prescribed by the Secretary. Such table shall be based on the prevailing commissioners' standard table (described in section 807(d)(5)(A)) used to determine reserves for group annuity contracts issued on the date as of which present value is being determined (without regard to any other subparagraph of section 807(d)(5)).

"(II) APPLICABLE INTEREST RATE.--The term 'applicable interest rate' means the annual rate of interest on 30-year Treasury securities for the month before the date of distribution or such other time as the Secretary may by regulations prescribe.

"(B) EXCEPTION.--In the case of a distribution from a plan that was adopted and in effect before the date of the enactment of the Retirement Protection Act of 1994, the present value of any distribution made before the earlier of--

"(i) the later of the date a plan amendment applying

subparagraph (A) is adopted or made effective, or

"(ii) the first day of the first plan year beginning after December 31, 1999,

shall be calculated, for purposes of paragraphs (1) and (2), using the interest rate determined under the regulations of the Pension Benefit Guaranty Corporation for determining the present value of a lump sum distribution on plan termination that were in effect on September 1, 1993, and using the provisions of the plan as in effect on the day before such date of enactment; but only if such provisions of the plan met the requirements of section 417(e)(3) as in effect on the day before such date of enactment."

* * *

(c) AMENDMENTS TO EMPLOYEE RETIREMENT INCOME SECURITY ACT OF 1974

<< 29 USCA § 1053 >>

(1) DETERMINATION OF PRESENT VALUE FOR PURPOSES OF RESTRICTIONS ON MANDATORY DISTRIBUTIONS.--Section 203(e)(2) of the Employee Retirement Income Security Act of 1974 (29 U.S.C. 1053(e)(2)) is amended to read as follows:

"(2) For purposes of paragraph (1), the present value shall be calculated in accordance with section 205(g)(3)."

<< 29 USCA § 1055 >>

(2) DETERMINATION OF PRESENT VALUE FOR PURPOSES OF RESTRICTIONS ON CASH- OUTS.--Section 205(g)(3) of such Act (29 U.S.C. 1055(g)(3)) is amended to read as follows:

"(3) DETERMINATION OF PRESENT VALUE.--

"(A) IN GENERAL.--

"(i) PRESENT VALUE.--Except as provided in subparagraph (B), for purposes of paragraphs (1) and (2), the present value shall not be less than the present value calculated by using the applicable mortality table and the applicable interest rate.

"(ii) DEFINITIONS.--For purposes of clause (i)--

"(I) APPLICABLE MORTALITY TABLE.--The term 'applicable mortality table' means the table prescribed by the Secretary of the Treasury. Such table shall be based on the prevailing commissioners' standard table (described in section 807(d)(5)(A) of the Internal Revenue Code of 1986) used to determine reserves for group annuity contracts issued on the date as of which present value is being determined (without regard to any other subparagraph of section 807(d)(5) of such Code).

"(II) APPLICABLE INTEREST RATE.--The term 'applicable interest rate' means the annual rate of interest on 30-year Treasury securities for the month before the date of distribution or such other time as the Secretary of the Treasury may by regulations prescribe.

"(B) EXCEPTION.--In the case of a distribution from a plan that was adopted and in effect prior to the date of the enactment of the Retirement Protection Act of 1994, the present value of any distribution made before the earlier of--

"(i) the later of when a plan amendment applying subparagraph (A) is adopted or made effective, or

"(ii) the first day of the first plan year beginning after December 31, 1999,

shall be calculated, for purposes of paragraphs (1) and (2), using the interest rate determined under the regulations of the Pension Benefit Guaranty Corporation for determining the present value of a lump sum distribution on plan termination that were in effect on September 1, 1993, and using the provisions of the plan as in effect on the day before such date of enactment; but only if such provisions of the plan met the requirements of section 205(g)(3) as in effect on the day before such date of enactment."

<< 26 USCA § 411 NOTE >>

(d) EFFECTIVE DATE.--

(1) IN GENERAL.--The amendments made by this section shall apply to plan years and limitation years beginning after December 31, 1994; except that an employer may elect to treat the amendments made by this section as being effective on or after the date of the enactment of this Act.

(2) NO REDUCTION IN ACCRUED BENEFITS.--A participant's accrued benefit shall not be considered to be reduced in violation of section 411(d)(6) of the Internal Revenue Code of 1986 or section 204(g) of the Employee Retirement Income Security Act of 1974 merely because (A) the benefit is determined in accordance with section 417(e)(3)(A) of such Code, as amended by this Act, or section 205(g)(3) of the Employee Retirement Income Security Act of 1974, as amended by this Act, or (B) the plan applies section 415(b)(2)(E) of such Code, as amended by this Act.

Pub. L. 105-34, 111 Stat. (Aug. 5, 1997)
Taxpayer Relief Act of 1997

* * *

<< 26 USCA § 411 >>

SEC. 1071. PENSION ACCRUED BENEFIT DISTRIBUTABLE WITHOUT CONSENT INCREASED TO $5,000.

(a) AMENDMENT TO 1986 CODE.--

(1) IN GENERAL.--Subparagraph (A) of section 411(a)(11) (relating to restrictions on certain mandatory distributions) is amended by striking "$3,500" and inserting "$5,000".

<< 26 USCA §§ 411, 417, 457 >>

(2) CONFORMING AMENDMENTS.--

(A) Section 411(a)(7)(B), paragraphs (1) and (2) of section 417(e), and section 457(e)(9) are each amended by striking "$3,500" each place it appears (other than the headings) and inserting "the dollar limit under section 411(a)(11)(A)".

(B) The headings for paragraphs (1) and (2) of section 417(e) and subparagraph (A) of section 457(e)(9) are each amended by striking "$3,500" and inserting "DOLLAR LIMIT".

(b) AMENDMENTS TO ERISA.--

<< 29 USCA § 1053 >>

(1) IN GENERAL.--Section 203(e)(1) of the Employee Retirement Income Security Act of 1974 (29 U.S.C. 1053(e)(1)) is amended by striking "$3,500" and inserting "$5,000".

<< 29 USCA §§ 1054, 1055 >>

(2) CONFORMING AMENDMENTS.--Sections 204(d)(1) and 205(g)(1) and (2) (29 U.S.C. 1054(d)(1) and 1055(g)(1) and (2)) are each amended by striking "$3,500" and inserting "the dollar limit under section 203(e)(1)".

HOUSE AND SENATE REPORTS

H.R. Rep. No. 93-807 (Feb. 21, 1974)

* * *

Because the objective is to encourage more adequate provision for retirement, plans are permitted to defer the payment of benefits to individuals with vested rights until they reach normal retirement age and are separated from the firm. [FN11]

* * *

FN11 However, to avoid requiring a plan to carry relatively small amounts of benefits on its books for a long period of time, the bill permits a plan to elect to pay off the employee's vested rights in the form of a lump-sum payment when the employee is separated if the amount of the distribution is less than $1,750.

* * *

H.R. Conf. Rep. No. 93-1280 (Aug. 12, 1974)

III. VESTING AND RELATED RULES (SECS. 203-209, 1012, 1015, 1021, 1022, AND 3032 OF THE BILL, AND SECS. 401, 411, AND 414 OF THE INTERNAL REVENUE CODE.)

A plan may provide for the "cash out" of an employee's accrued benefit. In other words, the plan may pay out, in a lump sum, the entire **value** of an employee's vested accrued benefit. . . .

A cash-out could be made from the plan without the employee's consent only if the payment (a) was made due to the termination of the employee's participation in the plan, (b) constituted the **value** of the employee's entire interest in the plan, and (c) did not exceed . . . $1,750 (with respect to the

value of the benefit attributable to employer's contributions).

. . .

A higher cash-out could be made with the employee's consent.

(emphasis added).

S. Rep. No. 98-575 (Aug. 2, 1984)

* * *

The committee on finance, to which was referred the bill (H.R. 4280) to amend the Employee Retirement Income Security Act of 1974 and the Internal Revenue Code of 1954 to improve the delivery of retirement benefits and provide for greater equity under private pension plans for workers and their spouses and dependents . . . reports favorably thereon with an amendment and recommends that the bill as amended do pass.

* * *

For purposes of determining the present value of the participant's benefit, the bill provides that a plan may not use an interest rate that is greater than the rate used by the Pension Benefit Guaranty Corporation (PBGC) for valuing a lump sum distribution upon plan termination.

* * *

For purposes of calculating the present value of a benefit as of the date of the distribution, the plan is required to use an interest rate no greater than the rate used by the Pension Benefit Guaranty Corporation (PBGC) in valuing a lump sum distribution upon plan termination. . . .

* * *

(emphasis added).

H.R. Conf. Rep. No. 99-841 (Sept. 18, 1986)

* * *

4. Cash-Out of Certain Accrued Benefits

Present Law

Under present law, in the case of an employee who separates from service, a pension, profit-sharing, or stock bonus plan may not immediately distribute any portion of the participant's benefit without the participant's consent, if the present value of the participant's accrued benefit exceeds $3,500 (sec. 411(a)(11) of the Code and sec. 203 of the Employee Retirement Income Security Act (ERISA)). **The interest rate used in determining the present value of a benefit for purposes of these cash out rules may not exceed the interest rate that would be used (as of the date of the distribution) by the Pension Benefit Guaranty Corporation (PBGC)** for purposes of determining the present value of a lump-sum distribution upon termination of the plan. The PBGC rate in effect at the beginning of a plan year may be used throughout the plan year if the plan so provides.

With respect to those plans subject to the automatic survivor benefit requirements (Code secs. 401(a)(11) and 417 and ERISA sec. 205), if the present value of the benefit under either the qualified joint and survivor annuity or the qualified preretirement survivor annuity exceeds $3,500, then the consent of the participant and spouse (or the surviving spouse if the participant has died) must be obtained before the plan can immediately distribute any part of the present value in a form other than a qualified joint and survivor annuity or a qualified preretirement survivor annuity. The interest rate used for determining the present value of a benefit may not exceed the interest rate that would be used (as of the date of the distribution) by the PBGC for purposes of determining the

present value of a lump sum distribution on plan termination. The PBGC rate in effect at the beginning of a plan year may be used throughout the plan year if the plan so provides.

House Bill

No provision.

Senate Amendment

The Senate amendment modifies the interest rate required to be used for purposes of determining the present value of (1) a participant's accrued benefit, (2) a qualified preretirement survivor annuity, or (3) a qualified joint and survivor annuity. Under the Senate amendment, a plan is required to compute the first $3,500 of the present value of a benefit by using an interest rate no greater than the interest rate (deferred or immediate, whichever is appropriate) that would be used by the PBGC (as of the date of distribution) upon the plan's termination. The remaining portion of the present value of the benefit is required to be determined using an interest rate no greater than 120 percent of the interest rate (deferred or immediate, whichever is appropriate) that would be used by the PBGC (as of the date of distribution) upon the plan's termination. The provision applies to distributions after December 31, 1984, except for distributions made after December 31, 1984, and before the date of enactment if such distributions were made in accordance with the regulations issued under the Retirement Equity Act of 1984.

Conference Agreement

The conference agreement follows the Senate amendment, except that a plan is required to use an interest rate no greater than the interest rate (deferred or immediate, whichever is appropriate) that would be used by the PBGC (as of the date of distribution) upon the plan's termination for purposes of determining whether (1) a participant's accrued benefit can be cashed out without consent because the present value of the vested accrued benefit is less than $3,500 and (2) the present value of a participant's vested accrued benefit is less than $25,000.

If the present value of the vested accrued benefit is no more than $25,000, then the amount **to be distributed** to the participant or beneficiary is calculated using the PBGC rate. If the present value of the accrued benefit exceeds $25,000 (using the PBGC interest rate), then the conference agreement provides that the amount **to be distributed** is determined using an interest rate no greater than 120 percent of the interest rate (deferred or immediate, whichever is appropriate) that would be used by the PBGC (as of the date of distribution) upon the plan's termination. In no event, however, is the amount **to be distributed** reduced below $25,000 when the interest rate used is 120 percent of the applicable PBGC rate.

For example, assume that, upon separation from service, the present value of an employee's total accrued benefit (including, e.g., any accrued benefits within section 411(d)(6) for which the employee is not yet eligible) is $50,000 using the applicable PBGC rate. Under the conference agreement, the plan may **distribute** to this employee (if the employee and, if applicable, the employee's spouse consents) the total accrued benefit, calculated using 120 percent of the applicable PBGC rate (e.g., **$47,000**).

* * *

H.R. Rep. No. 103-632(I) (Aug. 26, 1994)

* * *

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* * *

Subtitle F. Pension Plan Funding and Premiums
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* * *

SUMMARY OF H.R. 5110, THE "URUGUAY ROUND AGREEMENTS ACT"

H.R. 5110, the "Uruguay Round Agreements Act," approves the trade agreements resulting from the Uruguay Round of multilateral trade negotiations under the auspices of the General Agreement on Tariffs and Trade (GATT) and the Statement of Administrative Action (SAA) proposed to implement the Agreements, that were submitted to the Congress on September 27, 1994. . . . **The final two titles contain various provisions to offset the projected cost of the implementing legislation in order to comply with the pay-as-you-go requirements of the Budget Enforcement Act.**

* * *

TITLE VII-REVENUE PROVISIONS

* * *

Title VII also contains pension reforms that are designed to improve funding in current underfunded defined benefit plans guaranteed by the Pension Benefit Guaranty Corporation (PBGC) and to improve participant protections.

* * *

SUBTITLE F.-PENSION PLAN FUNDING AND PREMIUMS

I. Overview of present law

Defined benefit pension plans.-A defined benefit pension plan is a type of employer-sponsored retirement plan that provides benefits to participants based upon a formula specified in the plan. For example, a defined benefit pension plan could provide a benefit equal to a percentage of an employee's average compensation multiplied by the number of years of service with the employer. A defined benefit pension plan could also provide a flat dollar benefit based on years of service, or a specified percentage of final or average compensation. The key feature of such a plan is that the benefit promised is based on the plan formula, not on the assets or investment experience of the plan.

In order to help ensure that the promised benefits are paid to plan participants, defined benefit pension plans are subject to minimum funding requirements under both the Internal Revenue Code (the Code) and title I of the Employee Retirement Income Security Act of 1974, as amended (ERISA), which require the employer sponsoring the plan to make certain contributions to fund the plan. These requirements are discussed in detail below.

Pension Benefit Guaranty Corporation.-As enacted in ERISA, as well as under present law, the minimum funding requirements permit an employer to fund defined benefit pension plan benefits over a period of time. Thus, it is possible that a plan may be terminated at a time when plan

assets are not sufficient to provide all benefits earned by employees under the plan. In order to protect plan participants from losing retirement benefits in such circumstances, the Pension Benefit Guaranty Corporation (PBGC), a corporation within the Department of Labor, was created in 1974 by ERISA to provide an insurance program for benefits under most defined benefit pension plans maintained by private employers. According to the PBGC's annual report for fiscal year 1993, the single-employer insurance program covers more than 32 million participants in about 64,000 defined benefit pension plans.

Termination of underfunded pension plans.-Prior to 1986, an employer generally could, subject to contractual obligations, terminate a single- employer defined benefit pension plan at any time without regard to the financial health of the employer and without regard to the level of assets in the plan. If a single-employer defined benefit pension plan was terminated with assets insufficient to pay benefits at the level guaranteed by the PBGC, the employer was liable to the PBGC for the lesser of the insufficiency or an amount equal to 30 percent of the employer's net worth.

Under these rules, employers that wanted to rid themselves of unfunded liabilities could simply terminate the plan, and the PBGC would be liable for benefits. The PBGC was in some cases prevented from recouping its liability from the employer, even if the employer was financially sound. The plan termination rules were amended to prevent such transferring of liabilities to the PBGC by the Single-Employer Pension Plan Amendments Act of 1986 (SEPPAA) and were modified further by the Pension Protection Act of 1987.

Under present law, a defined benefit pension plan with assets insufficient to provide for benefit liabilities can be terminated voluntarily by the employer only if the employer and members of the controlled group of the employer are in financial distress (a distress termination). In general, benefit

liabilities include all fixed and contingent liabilities to plan participants and beneficiaries.

Following a distress termination, the PBGC pays out all benefits under the plan, including guaranteed benefits and those not guaranteed. The amount of benefits in excess of guaranteed benefits that are paid to plan participants depends on the level of plan funding and the amount the PBGC is able to recover from the employer. The employer is liable to the PBGC for the full amount of unfunded benefit liabilities.

Guaranteed benefits.-The PBGC guarantees vested retirement benefits (other than those that vest solely on account of the plan termination), up to a maximum benefit of $2,556.82 per month for plans terminating in 1994. The dollar limit is indexed annually for inflation. The guarantee is reduced for benefits starting before age 65, and does not apply to certain types of ancillary benefits. In the case of a plan or a plan amendment that has been in effect for less than 5 years before a plan termination, the amount guaranteed is generally phased in by 20 percent a year.

Sources of PBGC funding.-The PBGC is funded by assets in terminated plans, amounts recovered from employers who terminate underfunded plans, premiums paid with respect to covered plans, and investment earnings. All covered plans are required to pay a flat per-participant premium and underfunded plans are subject to an additional variable premium based on the level of underfunding.

As initially enacted in ERISA, covered plans were required to pay an annual flat premium to the PBGC of $1.00 per plan participant. The flat-rate per- participant premium has been increased several times since the enactment of ERISA, and is currently $19 per participant in 1994. The variable rate premium was enacted by the Pension Protection Act of 1987. It was believed that underfunded plans should bear a greater share of the premium than well-funded plans because they

pose a greater risk of exposure to the PBGC. The amount of the variable rate premium is $9.00 per each $1,000 of unfunded vested benefits, up to a maximum of $53 per participant. Thus, the maximum total per-participant premium for an underfunded plan is $72 per year.

II. Reasons for change

Financial status of the PBGC.-As of September 30, 1993, the PBGC reported a deficit of $2.9 billion in the single-employer insurance program. This is an increase over the $2.7 billion deficit reported as of the end of the prior fiscal year. The PBGC also estimated in its 1993 annual report that approximately $53 billion in unfunded liabilities existed in single-employer defined benefit pension plans in 1992. Approximately 72 percent of this underfunding, or approximately $38 billion, is concentrated in single-employer plans sponsored by just 50 companies, primarily in the steel, automobile, tire, and airline industries.

The PBGC has estimated its future financial status under a variety of assumptions. The single-employer program deficit could range from $1.9 billion by the end of 2003 if losses are relatively low, to $13.8 billion by the end of 2003 if losses are high.

In a study released by the U.S. General Accounting Office (GAO) in December 1992, [FN18] GAO reported that the 44 plans with the largest claims against the PBGC for calendar years 1986-88 had aggregate unfunded liabilities at termination of $2.7 billion. These unfunded liabilities were $990 million, or 58 percent, higher than the $1.7 billion in unfunded liabilities reported by the 44 plans on their last, pretermination annual filing with the Internal Revenue Service (IRS). GAO termed this additional unfunded liability a "hidden liability" to the PBGC because it was not reported by plans before termination.

Hidden liabilities can result from several causes. Most of the $990 million in hidden liability reported in the GAO study was due to PBGC's higher estimate of plan liabilities as a result of PBGC's use of actuarial assumptions that were different than the assumptions used by plan sponsors. Hidden liabilities also can result because of the payment of shutdown [FN19] or special early retirement benefits, earlier-than-anticipated retirements, and PBGC's receipt of fewer assets than reported by the plans.

Reasons for PBGC's financial status.-The chronic underfunding of some defined benefit pension plans poses a significant risk to the PBGC. The PBGC's single-employer insurance program has a $2.9 billion deficit. Furthermore, the overall level of underfunding is rapidly increasing among single employer plans and now exceeds $50 billion. Of this amount, reasonably possible future claims against the PBGC exceed $13 billion. These claims, and the continued underfunding of pension benefits threaten the future solvency of the PBGC and may lead to a taxpayer bailout if the Federal Government is required to pay pension benefits to participants of underfunded pension plans which terminate.

There is concern that the sponsors of underfunded defined benefit pension plans continue to promise additional pension benefits without funding the plans' existing unfunded pension liabilities. Under present law, new pension liabilities can be added to an underfunded defined benefit pension plan before old liabilities are funded. Companies in financial difficulty sometimes use benefit increases as a means to increase compensation when they cannot afford to pay higher current wages. Workers may be willing to accept such unfunded future pension promises because they are at least partially insured by the PBGC and workers recognize that the immediate costs to their employers of higher wages makes such wage increases unlikely.

Under present law, sponsors of underfunded defined benefit

pension plans are not required to fund their plans within a reasonable time. Under present law, plan sponsors are allowed to fund their pension liabilities over an extended period of time. Some companies have taken advantage of the flexibility under the present-law rules and have chosen to maintain their plans at significantly underfunded levels. Some companies have used this funding flexibility to maintain chronically underfunded plans whose financial condition has not improved since the passage of ERISA nearly 20 years ago. In a few cases, companies have terminated plans with no remaining assets without ever violating present-law minimum funding standards.

* * *

As reported by the GAO, following plan termination, plan underfunding typically is nearly 60 percent greater than previously reported by the plan sponsor on its latest Form 5500 filed with the IRS. In addition, the level of underfunding tends to rise rapidly shortly before termination of a defined benefit pension plan. . . .

The PBGC's deficit has increased, in part, because premiums paid to the PBGC are not sufficient to cover its operations. The PBGC's premium income continues to be insufficient to cover the costs of actual and expected plan terminations for which the PBGC is responsible. Further, the PBGC's variable rate premium does not properly reflect the risk assumed by the PBGC in providing insurance for severely underfunded defined benefit pension plans.

* * *

Results of bill.-The bill is designed to improve the funding of single-employer defined benefit pension plans and reduce the potential exposure of the PBGC. The bill also is intended to reduce or eliminate the PBGC's operating deficit and to reduce the defined benefit pension system's unfunded

liabilities for which the Federal Government is potentially responsible. . . .

III. Retirement Protection Act of 1994

A. PART I-PENSION PLAN FUNDING

1. Minimum funding requirements (secs. 751 and 761 of the bill, secs., 412(c), (l), and (m) of the Code, and secs., 204, 302 (d), and (e) of ERISA)

* * *

Normal cost.-The normal cost for a plan for a year generally represents the cost of future benefits allocated to the year by the funding method used by the plan for current employees and, under some funding methods, for separated employees. Specifically, it is the amount actuarially determined that would be required as a contribution by the employer to maintain the plan if the plan had been in effect from the beginning of service of the included employees and if the costs for prior years had been paid, and all assumptions as to interest, mortality, time of payment, etc., had been fulfilled. **The normal cost will be funded by future contributions to the plan** (1) in level dollar amounts, (2) as a uniform percentage of payroll, (3) as a uniform amount per unit of service (e.g., $1 per hour), or (4) **on the basis of the actuarial present values of benefits considered accruing in particular plan years.**

* * *

The accrued liability of a plan is the actuarial present value of projected pension benefits under the plan that will not be funded by future contributions to meet normal cost.

* * *

9. Single sum distributions (sec. 767 of the bill, secs. 411(a)(11), 417(e), and 415(b) of the Code, and secs. 203(e) and 205(g) of ERISA)

a. Determination of present value

Present law

Under the Code and ERISA, if the present value of a participant's nonforfeitable accrued benefit exceeds $3,500, the benefit cannot be distributed (i.e., cashed out) without the consent of the participant. In addition, if the present value of a joint and survivor annuity exceeds $3,500 it cannot be distributed without the consent of the participant and the participant's spouse. For purposes of these rules, present value is calculated by using an interest rate no greater than (1) the rate that would be used (as of the date of the distribution) by the PBGC for purposes of determining the present value of a lump-sum distribution on plan termination if the vested accrued benefit (using such rate) is not in excess of $25,000, or (2) 120 percent of such PBGC rate if the vested accrued benefit exceeds $25,000.

Explanation of provision

Under the bill, present value for purposes of the cash-out rules must be no less than the present value determined by using the mortality table that is to be prescribed by the Secretary of the Treasury based upon the "prevailing commissioners' standard table" used to determine reserves for group annuity contracts issued on the date as of which present value is determined. The prevailing commissioners' standard table means, with respect to any contract, the most recent commissioners' standard tables prescribed by the National Association of Insurance Commissioners which are permitted to be used in computing reserves for that type of contract under the insurance laws of at least 26 States when the

contract was issued (sec. 807(d)(5)(A) of the Code). Currently, the prevailing commissioners' standard table used to determine reserves for annuity contracts is the GAM 83 mortality table. Future changes in the prevailing table will only apply to the calculation of present value when the Secretary of the Treasury issues guidance making such changes applicable.

In addition, present value for purposes of the cash-out rules must be no less than the present value determined by using the annual rate of interest on 30-year Treasury securities for the month before the date of distribution or such earlier time as provided in Treasury regulations. The annual rate of interest on 30-year Treasury securities is the rate published by the Board of Governors of the Federal Reserve System.

A plan will not violate the prohibition on the reduction of accrued benefits merely because it calculates benefits in accordance with the provision.

Effective date

The provision is generally effective for plan years beginning after December 31, 1994, except that an employer can elect to treat the provision as being effective on or after the date of enactment.

Under a transition rule for distributions from plans in effect on the date of enactment of the bill, until the earlier of the first plan year beginning after 1999 or the later of when a plan amendment applying the provision is adopted or made effective, the bill requires present value to be calculated as under present law, using the interest rate valuation methodology for lump-sum distributions under PBGC regulations in effect on September 1, 1993, the present-law Code and ERISA rules, and the current plan provisions (provided they are consistent with present law).

* * *

Changes in interest rates and mortality assumptions

In general.-As under present law, the calculation of the deficit reduction contribution for underfunded plans is based on the plan's current liabilities. **Under the bill, a plan's current liability is determined as under present law, except that the bill (1) lowers the maximum interest rate that can be used to determine the current liability, and (2) requires all underfunded plans to use the same mortality table to determine current liability.**

Interest rate.-For plan years beginning on or after January 1, 1999, the bill reduces the highest permissible rate that may be used to calculate current liability to 105 percent of the weighted average of the rates of interest on 30-year Treasury securities during the 4-year period ending on the last day before the beginning of the plan year. For years beginning after 1994 and before 1999, the maximum permitted interest rate is the following percentage of such 4-year weighted average rate: plan years beginning in 1995, 109 percent; plan years beginning in 1996, 108 percent; plan years beginning in 1997, 107 percent; and plan years beginning in 1998, 106 percent.

Mortality tables.-Under the bill, in the case of plan years beginning after December 31, 1994, the mortality table used to determine current liability is to be prescribed by the Secretary based upon the 1983 Group Annuity Mortality Table (GAM 83 mortality table). Such mortality table will be effective until the later of plan years beginning in 2000 or such time as the Secretary prescribes new tables by regulations. . . .

H.R. Rep. No. 103-632(II) (Aug. 26, 1994)

Section 405-Single sum distributions

A plan must value a single-sum payment using an interest rate no greater than the applicable PBGC interest rate. (If the value exceeds $25,000, the interest rate must be no greater than 120% of the applicable PBGC rate.) PBGC regulations have been revised to change the methodology for calculating the applicable PBGC interest rate for terminated plans. The change in the regulations does not apply for purposes of determining the applicable interest rate for valuing single-sum payments. A plan may use any reasonable mortality table it specifies.

Congress adopted the interest rate cap to prevent plans from using unreasonably high interest rates to determine the present value of participants' benefits. If plans could use high interest rates, plans could lower the single sum paid to participants. The PBGC interest rates were adopted as the standard because the rates were presumed to duplicate group annuity rates. However, the PBGC interest rates reflect annuity rates only if considered in combination with specified PBGC mortality tables, and the law does not require that the specified PBGC mortality tables be used.

* * *

Sections 405(a) and 405(c) of the bill amend sections 203(e) and 205(g) of ERISA and sections 411(a)(11) and 417(e) of the Code to change the manner in which single sum distributions must be valued for purposes of these sections. Under the bill, single sum distributions may not be less than the amount that would be derived using the 30-year Treasury bond rate as of the date of distribution and a mortality table prescribed by the Secretary of the Treasury that is based on the prevailing Commissioner's standard mortality table used to determine reserves for group annuity contracts (currently the GAM 83

mortality table). Until the earlier of the 2000 plan year or the time the plan is amended to reflect this change, the bill requires single sum distributions from plans adopted and in effect before enactment of the bill to be calculated as under present law. The distributions must be calculated using the interest rate valuation methodology for lump sum distributions under PBGC regulations in effect on September 1, 1993 (but not the actual interest rate in effect on that date), and ERISA (or Code) and plan provisions in effect immediately before enactment, provided that the plan provisions complied with such prior ERISA or Code provisions.

* * *

OTHER AUTHORITATIVE MATERIALS

General Accounting Office Report, Private Pensions, Implications of Conversions to Cash Balance Plans No. GAO/HEHS-00-185 (Sept. 29, 2000)

Employer-provided pensions are an important source of income for many retired persons. To encourage employers to establish and maintain pension plans for their employees, the federal government provides preferential tax treatment under the Internal Revenue Code (IRC) for plans that meet certain requirements. The Joint Committee on Taxation estimates that in fiscal year 2000 the tax expenditure for qualified employer-sponsored pension plans will be about $76 billion. [n.1] **In exchange for preferential tax treatment, an employer is required to design the pension plan within legal limits that are intended to improve the equitable distribution and security of pension benefits.** There has been recent controversy concerning how conversions of traditional defined benefit pension plans to cash balance plans can affect workers, especially those nearing retirement. [n.2]

* * *

[W]e conducted a random sample survey of 420 firms on the 1999 Fortune 1000 list and reviewed pension plan documents to examine the features of cash balance plans. [n.3] **In addition, we conducted in-depth interviews with officials from 14 firms with cash balance or similar plans to discuss why they adopted such plans and to obtain information about how firms disclosed changes to their pension programs.** We modeled pension plan design features to compare pension benefits provided by a "basic" cash balance plan and defined benefit plan with a final average pay formula, common to large defined benefit plans. [n.4] **Also, we interviewed various federal agency officials, pension consultants, and actuaries. We conducted our work between September 1999 and August 2000 in accordance with**

generally accepted government auditing standards. . . .

* * *

Key reasons firms gave for converting include lowering total pension costs; adding a lump sum feature to increase the portability of pension benefits, thereby improving the firm's ability to recruit more mobile workers; and facilitating communication of the value of plan benefits. . . .

* * *

Conversions to cash balance plans can be advantageous to certain groups of workers–for example, to those who switch jobs frequently–but can lower pension benefits for others. **Cash balance plans provide a larger share of a participant's accumulated benefit earlier in a career, compared with a traditional defined benefit plan that is based on final average pay. As a result, conversions can increase the value of some workers' benefits, especially younger or short-tenured workers who leave firms before retirement. . . . Other workers, however, can be disadvantaged after conversion to a cash balance plan.**

Unlike traditional defined benefit plans, cash balance plans can result in a declining rate of normal retirement benefit accrual over time. This declining accrual rate can result in older workers' receiving lower benefits at retirement from a cash balance plan than they would have received from a traditional final average pay plan if it had not been converted. However, workers could also receive lower retirement benefits under a traditional plan if an employer reduces future accruals or terminates the plan. **Under some circumstances, conversions to cash balance plans can also result in periods during which some workers do not earn additional pension benefits while other workers continue to accrue benefits. These situations known as "wearaway," tend to last longer for older or long-tenured workers** and

occur because a participant's initial cash balance benefit is less than the value of the benefit accrued under the prior plan. . .

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* * *

Under defined contribution plans such as 401(k) plans, workers have individual accounts to which employers, employees, or both make periodic contributions. Defined contribution plan benefits are based on the contributions to and investment returns on these accounts. Employees bear the risk of poor investment performance and often control, at least in part, how the funds are invested.

Cash balance plans are referred to as hybrid plans because legally they are defined benefit plans but contain features that resemble defined contribution plans. Similar to traditional defined benefit plans, cash balance plans use a formula to determine pension benefits. However, cash balance plans express benefits as an "account balance." An employee account balance is based on hypothetical pay credits (percentage of salary or compensation) and hypothetical interest credits to employee accounts rather than an annuity. **As with other defined benefit plans, under cash balance plans, employee pension benefits are paid from commingled funds invested in a pension trust on behalf of all participants**, and plan trustees have a fiduciary responsibility for all assets in the pension trust. **Hypothetical account balances need not be related to investment returns on assets in the plan's pension trust, and hypothetical accounts are not credited with the plan's actual investment gains or losses. Employees neither own these "accounts" nor generally make investment decisions.** Cash balance plans are defined benefit plans because federal pension law defines any pension plan that does not provide individual accounts with benefits based solely on those accounts as a defined benefit plan. [n.8]

* * *

Prompted by concern from members of the Congress and charges by participants in plans that were converted, federal agencies are now reviewing age discrimination and other issues raised by cash balance plans. In September 1999, EEOC began a review of potential age discrimination issues in cash balance conversions and is coordinating with agencies that are responsible for administering federal pension laws. **Within the past year, more than 800 workers and retirees have filed age discrimination charges with EEOC concerning cash balance plans. EEOC has opened 34 cases to investigate these charges. The Department of the Treasury and IRS are currently reviewing tax qualification issues raised by cash balance plans. For example, in September 1999, IRS announced that is would begin requiring that applications for the approval of cash balance formula designs be forwarded to its headquarters for technical review, resulting in an effective moratorium on approving conversions to cash balance plans. . . .**

* * *

Firms adopted cash balance formulas for a variety of reasons, including reducing total pension costs, increasing portability to enhance the recruitment of younger or more mobile workers, and adding a lump sum feature that can be used to better explain pension benefits to workers. . . .

* * *

While we were told by pension practitioners, employer associations, and agency officials of firms' continuing interest in cash balance or similar hybrid plan designs, few of the firms we surveyed expected to adopt a cash balance plan in the future. . . . All of the firms considering adopting a cash balance plan told us that the continuing uncertainty as to whether such plans violate pension and age discrimination laws might discourage them from converting their plans.

* * *

Other firms told us, however, that they decided not to use cash balance plans because they had older or long-tenured workforces that could be adversely affected by a change to a cash balance plan.

Some firms we surveyed that chose to convert their plans cited the financial implications of changing to a cash balance plan as a key reason in their decision. Reducing the overall cost of the defined benefit plan was a primary reason some firms converted to a cash balance formula. For example, some firms have reduced costs by eliminating early retirement subsidies on future accruals. A PricewaterhouseCoopers survey of 100 cash balance plan sponsors found that 56 percent of firms expected the long-term cost of their defined benefit plans to decrease after conversion. . . .

Converting to cash balance plans is also an alternative to termination of a pension plan. Firms can terminate their defined benefit plans, but doing so imposes various economic costs. When plan sponsors terminate defined benefit plans, the sponsors must pay income and excise taxes on any surplus assets, immediately vest participants in their accrued benefits, and provide participants with annuities or lump sum payments. These costs may prevent some firms from terminating their plans. [n. 15] Instead, firms can convert to cash balance plans and achieve economic benefits from the surplus pension funds without incurring the costs related to plan termination. . . .

* * *

Most firms that expressed a desire to attract and hire more mobile workers as a reason for converting did not, however, change their vesting requirement when converting from a traditional defined benefit plan to a cash balance plan. As

under traditional defined benefit plans, workers under a cash balance plan must remain with a firm long enough to earn a right to such benefits. Large defined benefit plans typically have a "cliff" vesting requirement–that is, participants are 100 percent vested in their benefits after a certain number of years, with no rights to a pension benefit if they leave the firm before then. Most of these large plans have 100 percent vesting after 5 years. **Seventy-two percent of the firms we surveyed with cash balance plans had a 5-year cliff vesting requirement,** while the remaining firms sponsoring cash balance plans had various vesting requirements, including graded vesting. [n.17]

* * *

Conversions to cash balance plans can result in higher pension benefits accruing earlier in a worker's career and increase portability of benefits, which can be advantageous to younger or more mobile workers. However, the declining rate at which normal retirement benefits accrue in "basic" cash balance plan formulas (providing a level pay credit for all workers) can result in older workers receiving smaller annuities after conversion from a plan with a final average pay formula, assuming that the traditional plan remained unchanged. Conversions can also result in periods during which older workers accrue no new pension benefits while others do. While most Fortune 1000 firms in our survey that adopted cash balance plans have included transition provisions to mitigate the effects of plan formula changes on some participants, these provisions can vary in the extent to which they accomplish this objective.

* * *

Typically, participants under a defined benefit plan with a final average pay formula accrue the greatest share of their benefits in the final years of their careers because benefits are based on completed years of service and final average

salary, both of which usually increase as workers age. Generally, under a cash balance plan, the basis for determining benefits payable at normal retirement age includes both the hypothetical account balance (annual pay and interest credits) accrued to date plus the value of future hypothetical interest credits each pay credit would earn up to the plan's normal retirement age. As shown in figure 2, **workers under a cash balance plan who have many years before reaching normal retirement age earn a greater proportion of their benefits early in their careers.**

* * *

Cash balance plans can result in a decreasing rate at which normal retirement benefits accrue over time. The rate at which normal retirement benefits accrued in both defined benefit final average pay plans and cash balance plans depends on the number of years participants have remaining until they reach the plan-specified normal retirement age. However, in defined benefit plan with a final average pay formula, the rate of normal retirement benefit accrual increases as participants age, being driven by growth in service and wages. **As with defined benefit plans, under the law, the accrued benefit in cash balance plans must be expressed as an annual benefit beginning at normal retirement age. Cash balance plans must express benefits in this manner to comply with defined benefit plan rules.** [n.20] **For purposes of satisfying these rules, employee hypothetical accounts are not equal to the accrued benefits participants are entitled to receive. As a result, cash balance plans cannot simply provide participants hypothetical account balances as their benefit. Instead, the hypothetical balance must be calculated to comply with defined benefit plan accrual and other requirements.**[1]

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[1] [n.21 in text] In a calculation of the actual benefit, the hypothetical account balance is projected forward with interest earnings to the plan-specified normal retirement age. Next, the projected balance is converted into a normal

When a worker's hypothetical account balance in a given year is projected forward with hypothetical interest to normal retirement age, the rate of normal retirement benefit accrual declines as the employee ages, because each additional year's pay credit will have one less year in which future interest will compound. . . .

* * *

Our comparative design scenarios illustrate the declining rate of normal retirement benefit accruals inherent in cash balance plans. [n.22] The basic cash balance plans we simulated add annuity benefits to a participant's total pension benefit at smaller dollar increments each year that the participant ages.[2]

* * *

A cash balance plan's declining rate of normal retirement benefit accrual as workers age is the reason some have charged that these plans are age discriminatory. . . .

* * *

As with traditional defined benefit plans, workers must meet a plan's vesting requirement before they have a right

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retirement age annuity, using a plan-specified discount rate and mortality assumptions. Finally, the value of the annuity is discounted back to current dollars, using the assumptions for mortality and interest specified by federal regulations, to convert the normal retirement age annuity into an actuarially equivalent lump sum in current dollars.

[2] [n.23 in text] We measure the rate of benefit accrual by calculating the incremental annuity benefit added by the traditional final average pay and cash balance formulas each year to the total annuity benefit. The incremental annuity added by both formulas for a given year is determined by subtracting the total annuity benefit of the previous year from the total annuity benefit of the current year. . .

to their accrued pension benefit. BLS [Bureau of Labor Statistics] reported that median tenure among all workers aged 25 and older was 4.7 years in 1998, indicting that some workers change jobs before vesting. As we discussed earlier, most cash balance plans, like many traditional defined benefit plans, have a 5-year vesting requirement. Plan sponsors we interviewed told us that the 5-year vesting requirement of many cash balance plans results in some short-term, mobile workers' not benefitting from the higher benefits provided by cash balance plans because they leave before vesting and forfeit their accrued benefits.

* * *

Depending on the age of a participant at conversion and a plan's design features, conversions of defined benefit plans with final average pay formulas to cash balance plans can result in lower annuities for some participants than they would receive if no conversion occurs. . . . After conversion, the decreasing rate of normal retirement benefit accrual in the basic cash balance plan we modeled produces a lower annuity at retirement compared with the annuity benefit that traditional final average pay formula would generate. For example, **a 45-year-old worker at the time of conversion receives an annual annuity of about $18,500 at retirement from the cash balance plan instead of the $39,800 annuity the worker could have received from the defined benefit plan with a final average pay formula.** [n.31] **Likewise, a worker 50 years old at conversion receives an annual annuity of about $17,800 from the cash balance plan rather than the $35,100 annuity the final average pay formula could have provided.** For all workers we modeled, conversions to the basic cash balance plan resulted in lower annuities at the plan's normal retirement age than resulting from the final average pay formula.

For workers with equal salary and tenure at conversion, the basic cash balance plan we modeled produces the lowest

annuity at retirement for the worker who was oldest at conversion. This results from older workers having fewer years after conversion to earn benefits from the cash balance formula and a lower rate of normal retirement benefit accrual compared with the prior final average pay formula. **For example, we modeled benefits from a basic cash balance formula for a 35-, 45-, and 55-year-old worker with equal salary and tenure at conversion.** [n.32] Conversion to the cash balance plan resulted in lower annuities for each of these workers compared with the annuities they would have received had no conversion occurred. **The rate of normal retirement benefit accrual generated by the cash balance plan is lowest for the 55-year-old worker** (se fig. 5).

* * *

Conversions to cash balance plans sometimes result in "wearaway" situations in which some workers do not earn additional pension benefits after conversion while other workers continue to accrue benefits. [n.33] A wearaway period is created at conversion when a participant's opening hypothetical account balance is set at less than the present value of his or her prior accrued benefits–that is, the amount benefits would currently equal if paid out as a lump su. During wearaway, hypothetical pay and interest credit contributions do not represent new pension accruals until the cash balance account exceeds the value of benefits accrued under the prior formula. This is because workers who leave a firm during a wearaway period are entitled to receive the higher benefit they had accrued under the old formula before conversion.

Wearaway established at conversion tends to be longer for older workers. For example, the basic cash balance plan we modeled as establishing opening account balances at less than the present value of prior accrued benefits generated a 2-year lump sum wearaway for a 35-year-old worker, a 4-year wearaway for a 45-year-old worker, and an 11-year wearaway

for a 55-year-old worker at conversion (see table 2). [n.34] This is because older workers generally accrue larger benefits before conversion. Thus, older workers must wait longer before their hypothetical balances catch up to the value of prior accrued benefits and new benefits begin to accrue. **Wearaway created at conversion is also problematic for older workers because these periods often occur during the years when the traditional formula would have provided the most favorable rate of pension benefit accrual for them had no conversion occurred.**

* * *

We also simulated several examples in which workers' salary and tenure were equal at conversion in order to determine whether the length of a wearaway created at conversion can differ for workers of different ages. [n.35] In most of these simulations, the length of a lump sum wearaway created at conversion was extended 1 to 20 years for workers with equal salary and tenure but different ages. For example, we found that a 45-year-old faces a 4-year wearaway at conversion, while a 55-year-old with the same salary and tenure at conversion faces a 6-year wearaway. Another simulation we modeled indicates that a 40-year-old worker faces a 3-year wearaway at conversion while a 50-year-old worker with the same salary and tenure faces a 4-year wearaway. **Although our simulations show that differences in wearaway periods based on age can be small, the older worker faces the longer wearaway at conversion in every instance in which a difference in wearaway periods emerged.**

* * *

Annuity wearaways can arise as a result of conversion to a cash balance formula, depending on the form of annuity benefit that the worker selects and the design of early retirement benefits in the prior formula. . . . **[I]f the prior formula had included a subsidized early benefit, the 45-**

year-old worker who elects to receive early retirement benefits at age 60 has a 9-year wearaway of the early retirement annuity benefit even if the opening balance is established with the mandatory 417(e) discount rate.

* * *

Summary plan descriptions (SPD) are another means of providing information to employees about how conversions to cash balance plans can affect their pension benefits. . . .

* * *

However, many of the SPDs we reviewed did not clearly explain that the cash balance accounts were hypothetical and that participants did not actually own individual accounts as in a 401(k) plan. About half of the cash balance plan SPDs we analyzed did not make any reference to the hypothetical nature of cash balance plan accounts. Not stating that the accounts are hypothetical or making claims that the cash balance accounts are similar to 401(k) plan accounts can prevent plan participants from understanding how cash balance plans work and the benefits they are entitled to receive. For example, without making reference to the hypothetical nature of cash balance accounts, one firm described its cash balance plan as a "personal retirement account" that grows on the basis of compensation credits and interest credits. Other summary plan descriptions or related plan information described cash balance plans in a similar manner, including providing illustrations of the growth in cash balance accounts alongside of examples of how 401(k) plan accounts can increase over time without explicitly explaining that participants did not "own" the cash balance accounts and did not control how the assets are invested.

* * *

(emphasis added; bracketed footnotes and material between asterisks, including footnotes, charts, tables and graphs, omitted)

[The GAO Report can be ordered by calling the GAO (202/512-6000), or by visiting the GAO's website: http://www.gao.gov]

Statement on the Plan Termination and Control Act of 1985

Thursday, June 6, 1985

99th Cong. 1st Sess.

131 Cong. Rec. E 2614

REFERENCE: Vol. 131 No. 74; Continuation of Senate Proceedings of June 5, 1985, Issue No. 73; and Proceedings of June 6, 1985, Issue No. 74

TITLE: STATEMENT ON THE PLAN TERMINATION AND REVERSION CONTROL ACT OF 1985

SPEAKER: HON. EDWARD R. ROYBAL OF CALIFORNIA IN THE HOUSE OF REPRESENTATIVES

TEXT:
Test that appears in UPPER CASE identifies statements or insertions which are not spoken by a Member of the Senate on the floor.

MR. ROYBAL. MR. SPEAKER, IN AN ATTEMPT TO ADDRESS THE PROBLEM OF OVERFUNDED PENSION PLAN TERMINATIONS BY EMPLOYERS WHICH DEPRIVE AMERICAN WORKERS AND RETIREES OF THEIR RETIREMENT INCOME SECURITY, I AM TODAY REINTRODUCING THE PLAN TERMINATION AND REVERSION CONTROL ACT OF 1985.

* * *

AN ABUSE NOTED IN PREVIOUS COMMITTEE HEARINGS AND RECOGNIZED AS AN ISSUE WITHIN THE ADMINISTRATION GUIDELINES HAS BEEN THE USE OF INORDINATELY HIGH INTEREST RATES APPLIED TO

LUMP-SUM DISTRIBUTIONS MADE TO PARTICIPANTS UPON TERMINATION. TESTIMONY BY ONE WITNESS BEFORE THE COMMITTEE INDICATED THAT BASED UPON HIS 12 YEARS OF SERVICE WITH HARPER & ROW PUBLISHERS HE HAD RECEIVED A LUMP-SUM DISTRIBUTION OF APPROXIMATELY $700 FOR HIS ACCRUED BENEFIT. UPON SEEKING A LIFE ANNUITY FROM AN INSURANCE CARRIER HOWEVER, HE RECEIVED A QUOTE OF APPROXIMATELY $7,000 TO SECURE SUCH AN ANNUITY. THE ADMINISTRATION HAS RESPONDED TO THIS ABUSE BY PROMULGATING A REGULATION THAT REQUIRES AN INTEREST RATE BE USED WHICH APPROXIMATES A MARKET OR ANNUITY RATE.

* * *

PLAN DOCUMENT
(relevant provisions, only)

Introductory Page

The Georgia-Pacific Corporation Salaried Employees Retirement Plan is hereby amended and restated to read as follows. This amended and restated plan (the "Plan") shall be effective as of January 1, 1989. **The purpose of the amendment and restatement of this plan is to satisfy the requirements of the Tax Reform Act of 1986 and subsequent legislation.**

The Plan was previously amended and restated on June 1, 1989 to convert the Plan to a cash balance **defined benefit** pension plan and this amended and restated plan was effective as of January 1, 1989. . . .

* * *

(emphasis added).

Article 1
Definitions

The following words and phrases as used herein shall have the following meanings, unless a different meaning is plainly required by context:

1.1 Accrued Benefit. Accrued Benefit means, as of the time of reference, a monthly amount of benefit, payable in the form of an increasing life annuity, commencing on a Participant's Normal Retirement Date, where the amount of such monthly benefit is the result of dividing the then credits to such Participant's Personal Account by the applicable factor from Section A of Appendix A.

* * *

1.5 Benefit Commencement Date. Benefit Commencement Date means for each Participant or Beneficiary, in the case of an annuity form of distribution, the first day of the first period for which an amount is payable as an annuity under this Plan and , in the case of a lump sum payment, the first date on which all events have occurred which entitle the Participant to payment under this Plan.

* * *

1.10 Company. Company means Georgia-Pacific Corporation, a Georgia corporation, and any successor to such corporation.

* * *

1.29 Normal Retirement Date. Normal Retirement Date means the date on which a Participant reaches his sixty-fifth (65^{th}) birthday.

* * *

1.32 Personal Account. Personal Account means the bookkeeping account maintained with respect to a Participant as described in Article 3.

1.33 Plan. Plan means the Georgia-Pacific Corporation Salaried Employees Retirement Plan as amended and restated effective January 1, 1989.

* * *

1.38 Qualified Election. Qualified Election means an election to waive the automatic joint and fifty percent (50%) surviving spouse increasing annuity described in Section 6.3(a). The election must be in writing on a form prescribed by and filed with the Plan Administrator, and shall be invalid without Spousal Consent. Revocation of a prior Qualified Election may be made by a Participant in writing without the consent of his Spouse at any time before the Participant's benefits

commence. The number of revocations and Qualified Elections shall not be limited.

* * *

1.41 Severance Date. Severance Date means the date as of which an Employee is deemed to have severed his relationship as an Employee . . .

1.42 Spousal Consent. Spousal Consent means either (a) the written consent by the Participant's Spouse to a Qualified Election (as defined in Section 1.38), designation of Beneficiary or similar action by the Participant, which consent acknowledges the effect of such election, designation or action on such Spouse, which is witnessed by a notary public and which may expressly permit further elections, designations or similar action by such Spouse or (b) "deemed consent" to any such election, designation or similar action where the Plan Administrator is satisfied that written consent cannot be obtained because there is no Spouse, because the Participant's Spouse cannot be located, or because of other circumstances which may be provided by applicable law. . . .

* * *

1.44 Trust Agreement. Trust Agreement means the trust agreement between the Company and the Trustee, established as part of the Plan for the purpose of funding benefits under the Plan, or any successor trust agreement or agreements.

1.45 Trust Fund. Trust Fund means all such money or other property which is held by the Trustee, pursuant to the terms of the Trust Agreement.

* * *

Article 3
Participants' Personal Accounts and Credits to Personal Accounts

3.1 Establishment of Personal Accounts.
(a) A Personal Account shall be established and maintained for each Participant to which credits shall be made in accordance with the provisions of this Article 3. The Personal Accounts established and maintained pursuant to this Article 3 are intended to be bookkeeping accounts. Neither the establishment of such Personal Accounts nor the accrual of credits to such personal Accounts shall be construed as an allocation of assets of the Plan to, or a segregation of such assets in, such Personal Accounts, or otherwise as creating a right in any person to receive specific assets of the Plan. Benefits provided under the Plan shall be paid from the general assets of the Plan in the amounts, in the forms and at the times provided in Articles 4, 5 and 6.

* * *

3.2 Basic Monthly Credits for Service after January 1, 1989.
The amount credited to a Participant's Personal Account pursuant to this Section 3.2 depends on the Participant's Compensation as an Eligible Employee for the applicable calendar month. Credits pursuant to this Section 3.2 shall begin as of the end of the calendar month which begins on or after January 1, 1989 or which includes the date the Eligible Employee became a Participant, whichever comes last, and shall stop after the calendar month in which the Participant's Severance Date occurs. The amount of monthly credits to the Personal Account of an eligible Participant shall be equal to four percent (4%) of the Participant's Compensation for that calendar month as determined by the Plan Administrator. . .

* * *

3.5 Periodic Adjustments.

(a) Beginning January 1, 1990, and during each Plan Year after 1989, each Participant's Personal Account shall be automatically increased as of the end of each calendar month during the Plan Year in the manner described in Section 3.5(b) by a Periodic Adjustment Percentage calculated as follows:

(1) Determine the PBGC twelve (12) month average immediate annuity interest rate for the calendar year preceding the year in which the adjustment is to be made;

(2) Add to (1) 0.75%;

(3) Divide the sum of (1) and (2) by twelve (12); and

(4) Round the result to six (6) decimal places.

When referenced in this Plan, "annual periodic Adjustment Percentage" shall mean the Periodic Adjustment percentage calculated above in this subsection (a) multiplied by 12.

(b) Until the Benefit Commencement Date, each Personal Account shall be adjusted as of the end of each calendar month by an amount equal to the product of the Periodic Adjustment Percentage for the applicable Plan Year and the Personal Account balance at the beginning of such month. No adjustment shall be made under this Section 3.5 for any calendar month which includes the Benefit Commencement Date for any Personal Account.

* * *

Article 4
Retirement Benefits

* * *

4.5 Vested Benefit. If a Participant, who is not eligible for a retirement benefit in accordance with Sections 4.1, 4.2, 4.3 or 4.4, terminates employment after completing at least five (5) years of Service, he shall be entitled to receive a benefit equal to his then Accrued Benefit payable in accordance with the provisions of Article 6. . . .

* * *

Article 6
Payment of Benefits

* * *

6.2 Standard Benefit. The normal form of benefit payable to a Participant who is not married at his Benefit Commencement Date is an increasing annuity for the life of the Participant, the amount of which is determined as follows:
(a) The monthly payment in the Plan Year of his Benefit Commencement Date is determined in accordance with Section A of Appendix A.
(b) The monthly payment in the following Plan Year is equal to the amount determined under subparagraph (a) increased by the monthly Periodic Adjustment Percentage for that Plan Year times the number of monthly payments made in the preceding Plan Year.
(c) The monthly payment in each subsequent Plan year is equal to the monthly amount payable in the preceding Plan year increased by the annual Periodic Adjustment Percentage for the applicable Plan Year.

6.3 Standard Benefit for Married Participants.
(a) The normal form of benefit payable to a Participant who is married at his Benefit Commencement Date is a joint and fifty percent (50%) surviving spouse increasing annuity unless . . .
(b) Such joint and fifty percent (50%) surviving spouse increasing annuity shall be the Actuarial Equivalent (calculated pursuant to Section C of Appendix A) of the increasing annuity form described in Section 6.2 under which the Participant will receive a reduced annuity for his life, increasing as provided in Section 6.2 and ending with the payment for the month of his death; and if the person who was the Participant's Spouse on the Participant's Benefit Commencement Date survives the Participant, monthly

payments will be made to such Surviving Spouse beginning with the month after the month of his death for the Surviving Spouse's lifetime initially equal to fifty percent (50%) of the last monthly payment to the Participant and increasing thereafter as provided in Section 6.2.

* * *

(e) During the period commencing ninety (90) days before a Participant's Benefit Commencement Date, and ending not later than such Benefit Commencement Date, a Participant may waive his right to receive his benefit in the form of a joint and fifty percent (50%) surviving spouse increasing annuity, and elect instead to receive such benefit in the normal form described in Section 6.2, or in an optional form described in Section 6.4. Such waiver shall be made only by filing a Qualified Election with the Plan Administrator. . . .

6.4 Optional Forms of Benefit.
(a) An unmarried Participant, or a married Participant who has made an election under Section 6.3(e), may elect to receive, in lieu of the standard form of benefit in Sections 6.2 or 6.3, a benefit in one of the optional forms described below:

* * *

Option C: Lump Sum Payment. A single lump sum payment equal to the amount credited to the Participant's Personal Account as of the end of the month preceding his Benefit Commencement Date.

* * *

Article 7
Financing the Plan

7.1 Participant Contributions. Participants shall make no contributions under the Plan.

7.2 Employer Contributions. The Employer shall make such contributions from time to time which it shall deem necessary to provide the benefits of this Plan in accordance with generally accepted actuarial principles. . . .

7.3 Funding Policy. The Company shall be responsible for establishing and reviewing periodically a funding policy and method for the Plan, and in connection therewith to adopt and revise from time to time such actuarial assumptions and funding methods to be used in all actuarial calculations which may be required in connection with the Plan and to receive and review the reports of an Enrolled Actuary.

7.4 Funding Medium. The Company has entered into a Trust Agreement and/or Group Annuity Contract which shall be part of the Plan. All payments made pursuant to this Article 7 shall be paid to the Trust Fund and/or Insurance Company in such manner as the Company shall determine from time to time. All such payments and increments thereon shall be held and disbursed in accordance with the provisions of the Plan, the Trust Agreement and any Group Annuity Contract as each shall be applicable in the circumstances. No person shall have any interest in, or right to, any part of the funds so held in the Trust Fund or funds which may be held by the Insurance Company, except as expressly provided in the Plan, the Trust Agreement and the Group Annuity Contract.

7.5 Actuarial Gains/Forfeitures. Actuarial gains and/or forfeitures, if any, arising from termination of participation, or from any other source, shall not be applied to increase the benefits any Participant would otherwise receive under the Plan, but shall be used to reduce Employer contributions becoming due thereafter.

* * *

Article 10
General Provisions

* * *

10.6 Qualified Defined Benefit Plan. The Employer intends that the Plan (including the Trust Agreement and the Group Annuity Contract forming a part thereof) shall be a defined benefit pension plan of an employer for the exclusive benefit of its employees or their beneficiaries as provided for in Section 501(a) of the Code.

* * *

Article 15
Merger of Certain Great Northern Nekoosa Plans

15.1 Plan Merger. Effective January 1, 1991 . . .the Retirement Plan for Salaried Employees of Great Northern Nekoosa Corporation . . . shall be merged into this Plan. After January 1, 1991, all participants in the named plans shall be transferred to, and become participants in, this Plan and will have their (and their beneficiaries') benefits determined under this Plan . . .

* * *

Appendix A
Determination of Various Actuarial Equivalents

SECTION A: Factors to Convert to Increasing Life Annuity
The monthly amount of a Participant's increasing annuity shall equal the credits in the Participant's Personal Account as of his Benefit Commencement Date divided by the applicable annuity value (as defined below), based on the Participant's age as of his Benefit Commencement Date.

If the Benefit Commencement Date is the first of the month following the Participant's sixty-fifth (65th) birthday, the applicable annuity value is 210. Otherwise, the applicable annuity value is 210 plus (or minus) 0.50 for each month that the Benefit Commencement Date is before (or after) the first of the month following the Participant's sixty-fifth (65th) birthday.

SECTION B: Level Annuity

A Participant's level annuity shall be the single life annuity benefit which is the Actuarial Equivalent of the Increasing Life Annuity in Section A, as determined in accordance with Section D below, based on the credits in the Participant's Personal Account as of his Benefit Commencement Date.

SECTION C: Joint and 50% Survivor Annuity; Joint and 100% Survivor Annuity

A Participant's Joint and 50% Survivor Annuity, or his Joint and 100% Survivor Annuity, whichever is applicable, shall be the contingent annuity benefit which is the Actuarial Equivalent of the Increasing Life Annuity in Section A, as determined in accordance with Section D below, based on the credits in the Participant's Personal Account as of his benefit Commencement Date.

SECTION D:

Except as otherwise provide in this Plan, actuarial equivalence shall be determined using (1) the 1971 Group Annuity Table, blended 80% male and 20% female for a Participant and 80% female and 20% male for a Participant's Spouse or Contingent Annuitant, and (2) an interest rate equal to the immediate annuity rate set by the Pension Benefit Guaranty Corporation in its regulations under Section 4062 of ERISA, and (3) such other actuarial factors and methods as the Enrolled Actuary for this Plan recommends to the Company as reasonable and appropriate under the circumstances.

June 27, 1997 Amendment to the Plan

AMENDMENT NUMBER ONE
TO THE
GEORGIA-PACIFIC CORPORATION
SALARIED EMPLOYEES RETIREMENT PLAN
(As Amended and Restated Effective January 1, 1989)

THIS AMENDMENT to the GEORGIA-PACIFIC CORPORATION SALARIED EMPLOYEES RETIREMENT PLAN (the "Plan"), effective as stated below and adopted this 26th day of June, 1997, by GEORGIA-PACIFIC CORPORATION, a Georgia corporation ("G-P");

WITNESSETH:

* * *

WHEREAS, G-P desires to amend the Plan to change the Periodic Adjustment Percentage to comply with recent guidance issued by the Internal Revenue Service with respect to cash balance plans;

* * *

NOW, THEREFORE, in consideration of the premises, the Plan is hereby amended as follows:

* * *

3. Section 3.5(a) of the Plan is hereby amended effective as of January 1, 1996 to read as follows:

"(a) Beginning January 1, 1990 and during each Plan Year after 1989, each Participant's Personal Account shall be automatically increases as of the end of each calendar month during the Plan year in the manner described in Section 3.5(b) by a Periodic Adjustment Percentage calculated as follows:

(1) For Plan Years beginning after December 31, 1989 and before January 1, 1996

(A) Determine the PBGC twelve (12) month average immediate annuity interest rate for the calendar year preceding the year in which the adjustment is to be made;

(B) Add to (A) 0.75%; and

(C) Divide the sum of (A) and (B) by twelve (12).

(2) For Plan Years beginning after December 31, 1995, determine the monthly rate which will effectively yield on an annual basis, when compounded, the annual 30-year Treasury Constant Maturities rate published by the Federal Reserve Board for November of the calendar year immediately preceding the year in which the adjustment is to be made.

The Periodic Adjustment Percentage calculated under this Section 3.5(a) shall be rounded to six (6) decimal places."

* * *

(bolded emphasis added)

DOCUMENTS RELATING TO MR. LYONS' ADMINISTRATIVE CLAIM

Letter from Georgia-Pacific to Paul Holzman, dated April 17, 1996

Georgia-Pacific Corporation

Law Department

133 Peachtree Street, N.E.
P.O. Box 105605
Atlanta, Georgia 30348-5605
Telephone (404) 652-7388
Facsimile (404) 584-1461

Daniel R. Kopti
Senior Counsel

April 17, 1996

SENT VIA OVERNIGHT DELIVERY

Mr. Paul Holzman
National Center for Retirement Benefits, Inc.
666 Dundee Road, Suite 1200
Northbrook, IL 60062

Re: Mr. Jerry Lyons

Dear Mr. Holzman:

Your letter of March 18 to Ms. Becky Crockford has been referred to us for response.

We understand that Mr. Jerry Lyons is concerned about the interest rate used in calculating the lump sum distribution that he received in January 1993 from the Georgia-Pacific Salaried Employees Retirement Plan ("SERP"). He states in

your letter that the Plan Administrator for the SERP must calculate the present value of normal retirement benefits by using an interest rate permitted under Code Section 417(e) and IRS regulation 1.417(e)-1. He asserts that an incorrect interest rate was used in his case, causing a reduction in his lump sum distribution. Your letter asks to have his SERP benefits recalculated and to have any additional amounts paid to him, along with interest.

Please be advised that the SERP is a special form of defined benefit plan known as a "cash balance" plan. As described in IRS Notice 96-8, a "cash balance" plan defines benefits for each employee by reference to the amount of the employee's hypothetical account balance. An employee's hypothetical account balance is credited with hypothetical allocations and hypothetical earnings determined under a formula selected by the employer and set forth in the plan. These hypothetical allocations and hypothetical earnings are designed to mimic the allocations of actual contributions and actual earnings to an employee's account that would occur under a defined contribution plan. Most cash balance plans are designed to permit, after termination of employment, a distribution of an employee's entire accrued benefit in the form of a single sum distribution equal to the employee's hypothetical account balance as of the date of the distribution.

According to the Plan Administrator's records, Mr. Lyons terminated employment in January 1991. He elected at that time to postpone receipt of his SERP benefits until a future date. During 1991 and 1992, his personal account was credited with hypothetical earnings (which the SERP calls "credit adjustments") equal to the average Pension Benefit Guaranty Corporation immediate annuity rate in effect for the previous

calendar year, plus 0.75%. The credit adjustment for 1991 was equal to 8.23%, while the credit adjustment for 1992 was equal to 7.71%, compounded monthly. **In November 1992, Mr. Lyons requested a lump sum distribution of his personal account in the SERP. The distribution took place in January 1993 and was equal to the hypothetical balance in his personal account of $36,109.15. Contrary to Mr. Lyons' assertion, his lump sum distribution was not calculated with reference to the present value of a normal retirement benefit or by using an interest rate that violated IRS requirements.**

During the past several months we have exchanged several letters on the issue of whether Mr. Lyons qualifies as a "participant" in the SERP. As stated previously, the Supreme Court concluded in Firestone Tire and Rubber Co. v. Bruch, 489 U.S. 101, 117 (1989) that former employees who have no reasonable expectation of returning to covered employment can qualify as "participants' in an employee benefit plan only if they have a colorable claim to vested benefits. We are not persuaded that Mr. Lyons' claim for SERP benefits, as expressed in your letter of March 18, constitutes a colorable claim to vested benefits. However, in the interest of alleviating Mr. Lyons' concerns and as an expression of its good faith in this matter, the Plan Administrator for the SERP has decided to provide you with the summary plan description for the SERP. Also, if you would like a copy of the plan document, please send us a check in the amount of $28.75 to pay for photocopying charges (at the rate of 25 cents per page), and the document will be sent to you. The check should be made payable to "Georgia-Pacific Corporation Salaried Employees Retirement Plan". The furnishing of these documents does not constitute an admission by the Plan Administrator that Mr. Lyons is a "participant" in the SERP.

If you have any additional questions or comments regarding this matter, we request that you direct them to our attention.

Very truly yours,

Daniel R. Kopti
Senior Counsel

Enclosure
93314

(emphasis added).

OTHER PERTINENT MATERIALS

Affidavit of James A. Talerico

[district court caption omitted]

The undersigned, being first duly sworn, deposes and states:

1. I am an adult resident of the state of Georgia and am competent to give the testimony set forth below. I offer this Affidavit in support of Defendants' Motion for Summary Judgment.

2. I am Chief Counsel, Benefits, for Georgia-Pacific Corporation and my business address is 133 Peachtree Street, N.E., Atlanta, Georgia 30303.

3. The testimony set forth below is based upon my personal knowledge and experience in the execution of my duties as Chief Counsel, Benefits for Georgia-Pacific Corporation.

4. In October 1988, Georgia-Pacific Corporation submitted to the Internal Revenue Service a proposed amendment to the Salaried Employee Retirement Plan ("SERP") at issue in this case to obtain a determination that the SERP, as amended, would continue to be a tax-qualified deferred compensation plan. The proposed amendment converted the SERP from a traditional defined benefit plan to a cash balance pension plan, effective January 1, 1989. A true and correct copy of the amended and restated SERP is attached hereto as Exhibit A.

5. In May of 1989, the Internal Revenue Service issued a favorable determination letter stating that the SERP, as amended, (as set forth in Exhibit A) would continue to comply with the tax qualification requirements of the Internal Revenue Code. A true and correct copy of the favorable

determination letter is attached hereto as Exhibit B. Pursuant to this favorable determination letter, in June of 1989, the SERP was amended and restated to become a cash balance pension plan effective January 1, 1989.

6. All participants in the SERP, including Mr. Lyons, have been issued a copy of the Summary Plan Description for the SERP. A true and correct copy of the relevant Summary Plan Description for the SERP is attached hereto as Exhibit C.

7. On March 31, 1995, the SERP submitted another application to the Internal Revenue Service for a determination that the SERP continued to be tax-qualified. A true and correct copy of the application letter is attached as Exhibit D.

8. On January 18, 1996, the Internal Revenue Service issued Notice 96-8.

9. In response to Notice 96-8, the SERP was amended, effective January 1, 1996, to adopt one of the interest crediting rates suggested in the Notice. A true and correct copy of the proposed Amendment No. One is attached as Exhibit E.

10. On July 31, 1996, the Company submitted proposed Amendment No. One to the Internal Revenue Service to reflect the change in the interest crediting rate. Proposed Amendment No. One clearly stated that the changes had been made "to comply with recent guidance issued by the Internal Revenue Service with respect to cash balance plans" and, by its terms, was effective January 1, 1996.

11. In May of 1997, the Internal Revenue Service issued a favorable determination letter, stating that the SERP would continue to be a tax-qualified employee benefits plan, provided proposed Amendment No. One was adopted by the Company. A true and correct copy of the favorable determination letter is attached as Exhibit F.

12. Amendment No. One to the SERP was timely adopted on June 26 1997. A true and correct copy of the signed Amendment No. One to the SERP is attached as Exhibit G.

_____

James A. Talerico

Sworn to and subscribed
before me this 6th day
of March, 1998.

_____

Notary Public

My commission expires:
Notary Public, Clayton County, Georgia
My Commission Expires Feb. 26, 2000

Supreme Court, U.S.
FILED
MAR 13 2001
OFFICE OF THE CLERK

No. 00-1234

IN THE

Supreme Court of the United States

GEORGIA-PACIFIC CORPORATION
SALARIED EMPLOYEES RETIREMENT PLAN AND
GEORGIA-PACIFIC CORPORATION,
Petitioners,

v.

JERRY L. LYONS, individually and on
behalf of all other persons similarly situated,
Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Eleventh Circuit

REPLY BRIEF OF PETITIONER

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March 13, 2001

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REPLY BRIEF OF PETITIONER

Respondent's Opposition diverts attention from the fundamental issue in this case: whether it is unlawful under ERISA for cash balance plan sponsors to provide former employees with the option of choosing to receive a "lump sum" distribution in the amount equal to their stated account balances. Respondent, and the decision below, rely on regulatory restrictions that either do not exist or do not apply, and they would force plans to use valuation rules that are neither legally required nor logically suited for cash balance plans. This starkly violates ERISA's principle that employers are free to choose whether to have an employee benefit plan at all and, if so, what kind of benefits will be provided. It violates Congress's directive that the parallel standards of ERISA and the Tax Code be interpreted and applied consistently. And, it violates the principle that parties are entitled to fair notice of government regulations that could expose them to liability.

The Opposition's inconsistent assertions attempt to conceal the absence of any statutory or regulatory text imposing a "project-forward" requirement and prohibiting the Plan's lump sum provision. Respondent's convoluted explanations underscore the need for this Court's review to correct the decision below and thereby restore a basic precept of ERISA – "That the private parties, not the Government, control the level of benefits." *Alessi* v. *Raybestos-Manhattan, Inc.*, 451 U.S. 504, 511 (1981).

ARGUMENT

Respondent suggests the petition presents no new or compelling issues. This is wrong. As noted in the briefs of *amici*, the issues presented here are of enormous importance and concern to the employers and employees of this country. If uncorrected, the error of the decision below will "have a chilling effect on the development and maintenance of private

employer pension plans across the U.S. economy." NAM/ ABC Br. 6-7; see also Unifi/Towers Br. 3 (the decision below "makes it difficult if not impossible for cash balance plans to operate as intended"). Moreover, as the General Accounting Office ("GAO") has found, although most companies have considered adopting cash balance plans, many firms describe "uncertainty about possible changes in the regulations of cash balance plans" as a "[k]ey reason[]" for not adopting such a plan. GAO, *Cash Balance Plans: Implications for Retirement Income* 5 (2000), *available at* http://www.gao.gov/new.items/he00207.pdf ("*GAO Report*").[1]

The IRS has issued favorable determination letters to this Plan and to many other cash balance plans that do not incorporate the whipsaw valuation rule, but in 1996 issued Notice 96-8, a tentative guidance document that contemplates making the Plan, and others like it, illegal. The IRS's vacillating stance has provided little or conflicting guidance as to the legal requirements for cash balance plans. Not surprisingly, the GAO found in its review of cash balance plans that "no SPD [Summary Plan Description] explained that there was a difference between the hypothetical account balance [under a cash balance plan] and the accrued benefit. In fact, some SPDs specifically stated that the account balance was equivalent to the accrued benefit [as Petitioners' Plan does in its lump sum provision]." *GAO Report* at 38. Significantly, the GAO did *not* conclude that any plan violated ERISA or any Treasury or Labor Department regulation because it provided – like Petitioners' Plan – that account balances were "equivalent" to accrued benefits.

---

[1] The Opposition unfairly and inaccurately vilifies cash balance plan conversions. Opp. 7. There is no evidence (or allegation) that the Plan reduced future benefits for Mr. Lyons or other participants. Indeed, Respondent perversely seeks to make a fault of the Plan's generosity by arguing that ERISA is violated "if the plan's interest crediting rate *exceeds* the applicable discount rate." *Id.* at 6 (emphasis added).

Under these circumstances, Petitioners and similarly situated plan sponsors are stuck in a legal limbo that supports the grant of review. Petitioners never received fair notice of the purported regulatory restraint prohibiting them from adopting the lump sum benefit at issue here, and the Court's review could clarify the rule of *Alessi* that private parties are free to set the terms of their pension plans and confirm that what ERISA does not explicitly prohibit, it permits. See also *Lockheed Corp.* v. *Spink*, 517 U.S. 882, 887 (1996) (ERISA does not mandate what kinds of benefits employers must provide if they choose to provide benefits).

A. Respondent Received The Full Benefits To Which He Was Entitled.

As the Seventh Circuit recently held in affirming the dismissal of a class action suit under ERISA, "since [the employee] received the full benefits to which the plan documents entitled him, he has no basis for complaining of a violation of the terms of the plan or a forfeiture of vested benefits." *Brengettsy* v. *LTV Steel (Republic) Hourly Pension Plan*, No. 00-2204, 2001 WL 195204, at *3 (7th Cir. Feb. 28, 2001). That, of course, is precisely the case here.

The Plan documents expressly provide, as an "optional form of benefit," that a participant may elect to receive a lump sum distribution equal to his or her account balance – a benefit that does not include interest credits projected forward to retirement. The Plan states unequivocally:

> Option C: *Lump Sum Payment.* A single [l]ump sum payment equal to the amount credited to the [p]articipant's Personal Account as of the end of the month preceding his Benefit Commencement Date.

Plan § 6.4 (Pet. App. 74a). The definition of "Benefit Commencement Date" also could not be clearer:

> Benefit Commencement Date means for each Participant or Beneficiary, in the case an annuity form of

> distribution, the first day of the first period for which an amount is payable as an annuity under this Plan and, in the case of a lump sum payment, the first date on which all events have occurred which entitle the Participant to payment under this Plan.

Plan § 1.5 (Opp. App. A-123). Respondent concedes that he "waiv[ed] the annuity form of benefit and elect[ed], instead, a lump sum." Opp. 10. Under the clear terms of the Plan, this means he voluntarily requested and received a "[l]ump sum payment equal to the amount credited to [his] Personal Account as of the end of the month preceding his Benefit Commencement Date," (Pet. App. 74a) which "in the case of a lump sum payment, [is] the first date on which all events have occurred which entitle the Participant to payment under this Plan" (the date Respondent requested a lump sum distribution of his vested benefits) (Opp. App. A-123). Respondent voluntarily chose to receive the distribution of his account balance as expressly provided under Plan § 6.4(C). See Opp. 23 n.18. Like the plaintiff in *Brengettsy*, Respondent received the full benefit to which he was entitled and thus "has no basis for complaining."

B. The Plan Does Not Require Interest Credits To Be Projected Forward.

Respondent has not cited any specific Plan provision requiring interest credits to be projected forward. He cannot do so because there is no such provision. Respondent and the court of appeals erroneously rely on a provision for crediting account balances *left in the Plan* (Plan § 3.5(b) (Opp. App. A-126)), which provides as follows:

> Until the Benefit Commencement Date, each Personal Account shall be adjusted as of the end of each calendar month by an amount equal to the product of the Periodic Adjustment Percentage for the applicable Plan Year and

> the Personal Account balance at the beginning of such month.

Id.

Obviously, this provision does not provide for interest credits beyond the "Benefit Commencement Date," which, in the case of an optional lump sum benefit, occurs when the participant elects to receive it (almost always well before the normal retirement age of 65). See Plan § 1.5 (Opp. App. A-123) (quoted *supra* at 3-4). This is precisely why Respondent and the Eleventh Circuit rely so heavily on Notice 96-8 to bootstrap a "project-forward" requirement into the Plan.[2]

Respondent and the court of appeals make a basic mistake in confounding interest credits earned on account balances that remain invested in the Plan with interest projections for amounts withdrawn from the Plan. Rather than earning interest in the Plan, amounts withdrawn will earn interest (or other income) in whatever manner the former participant chooses to invest the distributed sums. There is nothing in the law or the Plan that entitles Respondent to double interest.

C. Respondent Fails To Refute The Plain Language Of ERISA § 203(e).

Respondent's Opposition makes it painfully obvious that, before the IRS's tentative "request for comments" in Notice 96-8, there was no statute or regulation in effect rendering the Plan or its lump sum provision unlawful. The Opposition makes lengthy and convoluted efforts to impose general

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[2] Ironically, the Opposition argues that the Plan itself (Appendix A, Section D (Opp. App. A-131)) provides for the use of the PBGC immediate annuity rate, not the interest crediting rate, to determine "actuarial equivalence," both for projecting forward and discounting back. Opp. 24. Thus, even under Respondent's argument regarding "actuarial equivalence," the Plan would project forward at the PBGC immediate rate and, as the Eleventh Circuit noted, pay Mr. Lyons the amount of his account balance – exactly what he received. Pet. App. 4a, 6a.

interest rate restrictions on voluntary lump sum distributions by cash balance plans.[3] Opp. 13-20. But while Respondent argues (correctly) that the purpose of § 203(e) is to prevent employers from manipulating discount rates to minimize lump sum distributions under defined benefit plans, Respondent is the one manipulating § 203(e) and conjuring up a "project-forward" requirement for the purpose of generating a windfall.

In any event, ERISA § 203(e)'s text does not limit the right of plans to include optional lump sum benefits in the amount equal to the participant's account balance. The statute solely addresses discount rates for present value purposes to determine whether distributions can be made without consent. As both the IRS and GAO have found, many or "most" cash balance plans do in fact provide for such lump sum payments, see I.R.S. Notice 96-8 (Pet. App. 60a-61a); *GAO Report* at 38, and the interest rate provisions of § 203(e) have not stopped the IRS from issuing favorable determination letters.

The Opposition is thus compelled to rely almost entirely on Notice 96-8, a tentative, prospective notice, issued by the IRS some three years *after* Respondent requested and received his lump sum distribution. Tellingly, neither the discount rate provisions of § 203(e), nor the publication of Notice 96-8 caused the IRS to withdraw the favorable determination letters issued to the Plan, or to "revoke the large numbers of favorable determination letters that it has issued cash balance plans that do not apply the whipsaw approach." Unifi/Towers Br. 14 n.11.

In fact, Notice 96-8 actually undermines Respondent's argument because the Notice recognized that "most" cash balance plans were designed just like Petitioners' Plan:

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[3] Respondent seems to bring a "psychic['s]" intuition to the laws and regulations, *see United States* v. *Chrysler Corp.*, 158 F.3d 1350, 1375 (D.C. Cir. 1998).

> *Most cash balance plans* also are designed to permit, after termination of employment, a distribution of an employee's entire accrued benefit in the form of a single distribution *equal to the employee's hypothetical account balance as of the date of the distribution*.

I.R.S. Notice 96-8 (Pet. App. 60a-61a) (emphasis added). The IRS's guidance was "prospective," did not indicate such "account balance" distributions were unlawful, and did not require (or even encourage) cash balance plans that were allowing lump sum distributions equal to account balances (like Petitioners') to change their plans. Not surprisingly, then, the GAO Report indicates that many plans have not conformed their lump sum provisions to the tentative guidance described in Notice 96-8. See generally, *GAO Report* at 38.

D. The Favorable IRS Determination Letters Cannot Be Dismissed.

Respondent fails to recognize the practical and legal significance of the determination letters issued to the Plan. In particular, Respondent mistakenly argues that determination letters only implicate a few, discrete sections of the Tax Code. See Opp. 25. A determination that a plan is "tax qualified" under § 401 necessarily requires a determination that the Plan satisfies many other Code provisions, including §§ 411 and 417. See, *e.g.*, 26 U.S.C. § 401(a)(7) and (11) (referencing §§ 411 and 417).[4] The IRS worksheets used by IRS personnel to verify a plan's tax qualification status confirm the

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[4] Respondent mistakenly relies on 26 C.F.R. § 601.201(o)(2) to call into question the favorable determination letters the IRS issued to the Plan. Respondent states that this regulation drains the letters of any approval regarding the statutory sections at issue in this petition. Opp. 25. For the reasons already discussed, that is absurd. Although the regulation suggests that a plan may not seek a determination letter as to certain Code sections in isolation, it does not limit the scope of the inquiry the IRS must undertake to determine whether a plan is "tax qualified."

broad scope of the inquiry – requiring, *inter alia*, that the IRS verify compliance with §§ 411 and 417. See, *e.g.*, IRS Form 5624, at V.g. (Pet. App. 77a) ("Does the plan satisfy the § 417 interest rate limitations . . . ?"), and at VI.a.-c. (*id.* at 77a-78a) (addressing § 411 vesting requirements).

Respondent relies on *Christensen* v. *Harris County*, 529 U.S. 576 (2000), to support his claim that IRS determination letters are entitled to "no deference." See Opp. 26 n.21. In *Christensen*, however, this Court recognized that agency interpretations and opinion letters are entitled to at least *Skidmore* deference – even if they do not qualify for full *Chevron* deference. *Christensen*, 529 U.S. at 587. Reasonable deference should be given to the IRS's original determination that the Plan satisfied all the requirements to be "tax qualified" here. The lump sum distribution provisions are clearly laid out in the Plan and comprise a key element of the Plan that the IRS would not reasonably have overlooked. Moreover, even if, as Respondent suggests, the IRS somehow "made a mistake" in issuing the determination letters (it did not), that would only confirm the regulatory uncertainty governing cash balance plans. Petitioners could not reasonably have been "on notice" of a "project-forward" requirement where the IRS has not adopted a formal regulation and, where the Agency itself has repeatedly confirmed the tax qualified status of the Plan as well as many other cash balance plans with similar lump sum provisions. See Unifi/Towers Br. 2-3.

E. *Firestone* Deference To Plan Administrators Does Not Affect The Standard For Appellate Review.

Respondent completely misunderstands *Firestone* deference and *de novo* appellate review. Opp. 20-21. Under *Firestone Tire & Rubber Co.* v. *Bruch*, 489 U.S. 101, 115 (1989), a court must defer to the reasonable interpretations of an ERISA plan made by an authorized plan administrator. Here, the Plan specifically authorizes the administrator to

interpret all provisions of the Plan, including the lump sum provision. Plan § 8.2 (Pet. App. 74a-75a); Holzman Letter (*id.* at 82a-85a). The court of appeals properly reviewed the district court's decision *de novo*, but the question here is entirely different: whether the court of appeals should have given reasonable deference to the Plan administrator's interpretation of the Plan's own terms. This issue was not briefed or argued before the district court and, indeed, could not have been, since it arose only when the court of appeals, *sua sponte*, chose to interpret the provisions of the Plan.

F. Respondent's Argument Undermines The Required Consistency Between ERISA And The Internal Revenue Code.

The Opposition fails to address – let alone refute – one of the central arguments made in the petition for certiorari: namely, that the Eleventh Circuit's decision opens a chasm between ERISA and the parallel provisions of the Tax Code, subjecting employers to inconsistent obligations under identically worded provisions. This dichotomy frustrates the clear congressional intent requiring consistency and predictability in the administration of employee benefit plans, and provides an important, additional reason why Supreme Court review is needed. See Unifi/Towers Br. 15-16 (Congress sought to limit conflicting regulatory requirements facing plan sponsors and fiduciaries under ERISA and the Internal Revenue Code).

G. Respondent Misapprehends Petitioners' Right To "Fair Notice" Of Potential Liability.

Respondent cites only Treasury Decision 8360 ("T.D. 8360") to support his argument that Petitioners had "considerable notice" of a "project-forward" requirement prior to Notice 96-8, concluding that T.D. 8360 "specifically informed cash balance plans that they must comply with the valuation rules under Code § 417(e) and TR 1.417(e)." Opp. 29 (emphasis omitted). To the contrary, T.D. 8360 actually reinforces the argument that the law does not require cash balance

plans to use a "project-forward" calculation. T.D. 8360 merely established a voluntary safe-harbor that cash balance plans could use to satisfy certain non-discrimination rules, not the interest rate provisions of § 203(e). As Respondent recognizes, the safe harbor was available to cash balance plans that "compl[ied] with the valuation rules applicable to defined benefit plans." *Id.* (emphasis omitted). T.D. 8360 thus establishes that cash balance plans were not ***required*** to conform to the valuation rules for defined benefit plans. Conformity was optional – necessary only if the plan chose to qualify for the non-discrimination safe harbor.

This was confirmed when the IRS issued Notice 96-8 as a request for comments so that the Agency could address the concerns and uncertainties raised by T.D. 8360 in future guidance. I.R.S. Notice 96-8 (Pet. App. 63a). Of course, the IRS never issued that guidance, and the rules applicable to cash balance plans remained unresolved. As the IRS, GAO, and the *amici* all recognize: many if not "most" cash balance plans still offer lump sum benefits like the one at issue, and numerous favorable determination letters for such plans remain outstanding. To this day, the IRS has never issued any regulation stating that cash balance plans may not provide optional lump sum benefits in an amount equal to the participant's account balance. If the Government ever tried to enforce the purported "project-forward" or "whipsaw" requirement against a cash balance plan, it would surely fail for lack of fair notice. See, *e.g.*, *General Elec. Co.* v. *EPA*, 53 F.3d 1324, 1333-34 (D.C. Cir. 1995). Given that Respondent unquestionably received what he was entitled to under the plain terms of the Plan, he has even less standing than the Government would have to impose liability on the Plan for this chimerical regulatory requirement.

CONCLUSION

For the foregoing reasons, the petition for certiorari should be granted.

Respectfully submitted,

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March 13, 2001

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In The
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October Term, 2000

Georgia-Pacific Corporation Salaried Employees Retirement Plan and Georgia-Pacific Corporation,

Petitioners,

v.

Jerry L. Lyons, individually and on behalf of all other persons similarly situated,

Respondents.

On Petition for a Writ of Certiorari to the United States Court of Appeals for the Eleventh Circuit

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MOTION FOR LEAVE TO FILE BRIEF AND BRIEF *AMICUS CURIAE* OF UNIFI NETWORK AND TOWERS PERRIN IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI

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March 2, 2001

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MOTION OF UNIFI NETWORK AND TOWERS PERRIN FOR LEAVE TO FILE A BRIEF *AMICUS CURIAE* IN SUPPORT OF THE PETITION FOR WRIT OF CERTIORARI

Unifi Network, a subsidiary of PricewaterhouseCoopers LLP ("Unifi Network"), and Towers Perrin hereby move, pursuant to Rule 37.2, for leave to file the attached brief *amicus curiae* in support of the petition for writ of certiorari in this case. While the petitioners have consented to the filing of this brief, respondent Jerry Lyons has declined to consent. Correspondence reflecting the consent of the petitioners has been lodged with the Clerk.

Unifi Network and Towers Perrin consult with and advise employers on how to provide retirement and other employee benefits to their employees. PricewaterhouseCoopers is the world's largest professional services organization, and Towers Perrin provides advice to approximately three-quarters of the *Fortune 1000*.

For several decades, amici have consulted with and assisted numerous employers in the adoption and maintenance of defined benefit pension plans to meet the employers' objectives and the needs of their employees. In recent years, amici have concluded that traditional defined benefit plan designs no longer meet those objectives and needs for an increasing number of employers, especially those with more dynamic and diverse workforces that are faced with mounting competitive pressures. Some of those employers have decided to curtail or terminate their defined benefit plans in favor of defined contribution plans. Other employers have decided to change their defined benefit plans to designs, such as a "cash balance" plan, that distribute benefits more evenly among employees, are better understood and appreciated by employees, and provide more flexibility in payment options.

Kwasha Lipton—now part of Unifi Network—developed the first cash balance plan, which was implemented by Bank of America in 1985. For more than fifteen years, amici have assisted numerous employers in designing and administering cash balance plans. Amici and other experts have met on many occasions with government regulators to provide advice and make suggestions on how to apply to cash balance plans the various tax-qualification and related rules under the Employee Retirement Income Security Act of 1974, as amended, 29 U.S.C. § 1001 *et seq.* ("ERISA"). To date, no

comprehensive, definitive regulatory guidance of general applicability has been issued addressing cash balance plans. Nevertheless, amici, cash balance plan sponsors, and other experts have derived substantial comfort that cash balance plans may be operated as they were designed and intended from the numerous favorable determination letters issued to cash balance plans by the Internal Revenue Service ("IRS"). Many of these letters approved cash balance plans having provisions that are substantially the same as those included in the Georgia Pacific plan and that have been rejected by the Eleventh Circuit's decision below.

For the past fifteen years, these IRS determination letters have been the only definitive expression from any government agency that specifically address the way in which cash balance plans are to satisfy the present value requirements at issue in this case. Cash balance sponsors had no other means of gaining comfort that their plans satisfied the ERISA requirements that directly parallel the Internal Revenue Code provisions. Furthermore, not until the Eleventh Circuit's decision below (and the almost simultaneous decision of the Second Circuit in *Esden v. Bank of Boston*, 229 F.3d 154 (2d Cir. 2000), *cert. dismissed,* 121 S. Ct. 674 (2001)) did any court conclude that cash balance plans cannot be operated in the manner in which they were designed. These court decisions have thereby disrupted the settled expectations of amici, cash balance plan sponsors, and the employees who participate in cash balance plans.

This case will have far-reaching effects on employee pension plan design and administration. Under the decision below, cash balance plans cannot be operated as intended nor in the forms that have previously been approved by the Internal Revenue Service. In addition, the Eleventh Circuit's decision would subject these plans to conflicting regulatory requirements. Unless the decision of the Eleventh Circuit is reviewed and clarified by this Court, the decision is sure to restrict the broad authority accorded employers to determine the way in which they provide retirement benefits to their employees. In addition, the failure of the Eleventh Circuit to accord any defer-

ence to determination letters issued by the IRS causes uncertainty that will discourage the voluntary adoption of pension plans by employers.

Because of the importance of these issues to Unifi Network, Towers Perrin, and defined benefit plan sponsors, and because of their extensive experience with the issues presented in this case, amici respectfully move for leave to file the attached brief *amicus curiae* to assist the Court in evaluating the petition for certiorari in this case.

Respectfully submitted,

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Dated: March 2, 2000

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Respondents.

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BRIEF OF UNIFI NETWORK AND TOWERS PERRIN AS *AMICI CURIAE* IN SUPPORT OF THE PETITION FOR WRIT OF CERTIORARI

Unifi Network, a subsidiary of PricewaterhouseCoopers LLP ("Unifi Network"), and Towers Perrin respectfully submit this brief *amicus curiae* in support of the petition for a writ of certiorari in this case.[1]

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[1] Counsel for Unifi Network and Towers Perrin authored this brief in its entirety. No person or entity, other than amici, made a monetary contribution to the preparation or submission of this brief.

INTERESTS OF AMICI CURIAE

Unifi Network and Towers Perrin consult with and advise employers on how to provide retirement and other employee benefits to their employees. PricewaterhouseCoopers is the world's largest professional services organization, and Towers Perrin provides advice to approximately three-quarters of the *Fortune 1000*.

For several decades, amici have consulted with and assisted numerous employers in the adoption and maintenance of defined benefit pension plans to meet the employers' objectives and the needs of their employees. In recent years, amici have concluded that traditional defined benefit plan designs no longer meet those objectives and needs for an increasing number of employers, especially those with more dynamic and diverse workforces that are faced with mounting competitive pressures. Some of those employers have decided to curtail or terminate their defined benefit plans in favor of defined contribution plans. Other employers have decided to change their defined benefit plans to designs, such as a "cash balance" plan, that distribute benefits more evenly among employees, are better understood and appreciated by employees, and provide more flexibility in payment options.

Kwasha Lipton—now part of Unifi Network—developed the first cash balance plan, which was implemented by Bank of America in 1985. For more than fifteen years, amici have assisted numerous employers in designing and administering cash balance plans. Amici and other experts have met on many occasions with government regulators to provide advice and make suggestions on how to apply to cash balance plans the various tax-qualification and related rules under the Employee Retirement Income Security Act of 1974, as amended, 29 U.S.C. § 1001 *et seq.* ("ERISA"). To date, no comprehensive, definitive regulatory guidance of general applicability has been issued addressing cash balance plans. Nevertheless, amici, cash balance plan sponsors, and other experts have derived substantial comfort that cash balance plans may be operated as they were designed and intended from the numerous favorable determination letters issued by the Internal Revenue Service ("IRS"). Many of these

letters approved cash balance plans having provisions that are substantially the same as those included in the Georgia Pacific plan and that have been rejected by the Eleventh Circuit's decision below.

SUMMARY OF ARGUMENT

Defined benefit pension plans cover approximately 47 million employees in the United States today. Collectively, these plans hold several trillion dollars in assets set aside to provide retirement benefits to American workers. Defined benefit plans historically have conformed to traditional plan designs. In many segments of the workforce, traditional plan designs fail to deliver meaningful retirement benefits to most employees covered by these plans, particularly women and lower-paid employees. Instead, benefits are concentrated on the relatively small segment of the workforce that spends all or most of a career, without interruption, at a single employer. Employers, both governmental and private, have taken steps in recent years to redesign their defined benefit plans to better address the needs of all their employees. The result has been a marked shift away from traditional plan designs to newer plan designs that distribute retirement benefits more equitably among employees. Cash balance plans have been at the forefront of this shift. Such plans now cover millions of employees at hundreds of employers, including roughly one in every five of the nation's largest private employers.

The issue in this case goes to the heart of whether defined benefit pension plans can provide more equitable benefits that do not conform to traditional plan designs. The decision of the court of appeals below adopts an interpretation of the statute that makes it difficult if not impossible for cash balance plans to operate as intended. This interpretation is unsound because it ignores the plain language of the statute, and because it forces cash balance plans to distribute benefits in a manner that not only undermines the employment relationship, but also violates the very provision of the statute the court of appeals sought to interpret. As a result, the decision improperly restricts the broad authority employers enjoy under federal law to determine the compensation and retirement benefits of their employees. Furthermore, the decision undermines the settled expectations of em-

ployers and employees alike as to the benefits that cash balance plans would provide and that the Internal Revenue Service previously had approved in numerous determination letters issued to individual plans, including the plan in this case.

Amici urge the Court to grant the petition for certiorari. A major portion of the nation's wealth is set aside in defined benefit pension plans. Employers should be free to use the assets they have accumulated in these plans to provide for the retirement needs of more of their employees. An interpretation of the statute that is faithful to its language is sufficient to achieve this important national objective.

REASONS FOR GRANTING THE WRIT

I. THE ELEVENTH CIRCUIT'S INTERPRETATION IMPROPERLY RESTRICTS THE BROAD AUTHORITY EMPLOYERS ENJOY UNDER FEDERAL LAW TO DETERMINE THE RETIREMENT BENEFITS OF THEIR EMPLOYEES.

ERISA and the Code[2] place solely and squarely in the hands of employers two critical decisions: whether to establish a pension plan at all and, once such a plan is established, what benefits to offer employees under the plan. As this Court has observed, "Nothing in ERISA requires employers to establish employee benefits plans. Nor does ERISA mandate what kind of benefits employers must provide if they choose to have such a plan." *Lockheed Corp. v. Spink*, 517 U.S. 882, 887 (1996).

The latitude granted employers to determine benefits is particularly broad in the case of a defined benefit pension plan. In contrast to a defined contribution plan, which is limited to providing

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[2] References in this brief to "ERISA" are to the Employee Retirement Income Security Act of 1974, as amended, 29 U.S.C. § 1001 *et seq.*, and references to the "Code" are to Internal Revenue Code of 1986, as amended.

benefits based solely on the contributions and earnings accumulated in individual participant accounts, a defined benefit plan is defined simply as "any plan which is not a defined contribution plan." *See* ERISA § 3(34)-(35), 29 U.S.C. § 1003(34)-(35); Code § 414(i)-(j). Thus, an employer that is willing to assume the greater liability of promising a defined level of retirement benefits (as opposed to limiting its liability to a defined level of contributions) is free to establish a defined benefit plan and to specify the type of retirement benefits the plan will provide.

For certain enumerated purposes, ERISA and the Code require the benefits otherwise specified by the employer in a defined benefit plan to be expressed as or converted into a traditional annuity commencing at normal retirement age. *See, e.g.*, ERISA §§ 3(23)(A), 204(b)(1)(C) (for purposes of testing benefit accruals for prohibited backloading), 29 U.S.C. §§ 1003(23)(A), 1054(b)(1)(C); *see also* Code § 411(a)(7)(A)(i), (b)(1)(C) (same); Treas. Reg. § 1.401(a)(4)-3(d)(1)(i) (for purposes of testing benefit accruals for prohibited discrimination). However, both statutes are clear that employers are free to define the benefits the plan will actually pay in ways other than as a traditional annuity beginning at normal retirement age. *See, e.g.*, ERISA § 204(c)(3) (discussing defined benefit plans in which "an employee's accrued benefit is to be determined as an amount *other than* an annual benefit commencing at normal retirement age" (emphasis added)), 29 U.S.C. § 1054(c)(3); Code § 411(c)(3) (same); Treas. Reg. § 1.411(a)-7(a)(1)(ii) (same); Treas. Reg. § 1.411(d)-6 Q&A-5(a)(1) (same).

In recent years, employers have begun to avail themselves of the flexibility afforded by defined benefit plans to define retirement benefits in ways other than as traditional deferred annuities. In particular, employers have been moving away from traditional plan designs to newer plan designs, such as cash balance plans, that define benefits in terms of a current lump sum value that grows steadily over time in a fair and equitable manner. Employers have been making this shift for good reason. As explained further below, for many employers these new plans address the retirement needs of their employees far better than plans based on traditional deferred annuities.

The decision of the Eleventh Circuit below would undermine the ability of employers to determine the benefits that cash balance plans actually pay. Worse still, the decision would force employers to add an unintended windfall benefit to cash balance plans that would (1) vary erratically from one year to the next, (2) diminish over time as younger employees age, (3) not be available in most cases to older employees at all, (4) thereby impose a substantial financial penalty on employees who continue employment with the sponsoring employer or who wait to begin receiving their benefits, and (5) threaten the funded status of many plans through a substantial, unanticipated increase in benefit liabilities.

That Congress could not possibly have intended this result is self-evident. There is no need, however, for recourse to Congressional intent to confirm the flaws in the Eleventh Circuit opinion, because the opinion overlooks the plain language of the statute. That language prescribes precisely how plans that define benefits in terms other than traditional deferred annuities are to comply with the provision of ERISA the Eleventh Circuit sought to interpret. By interpreting ERISA in a manner that is faithful to its language, this Court can restore to employers their rightful authority to determine the benefits they provide their employees under cash balance plans.

A. Employers That Adopt Cash Balance Plans Are Exercising Their Right to Provide Retirement Benefits That Fit the Needs of Their Employees Better than Traditional Defined Benefit Plans.

Employers that sponsor defined benefit plans have been shifting away from plans that provide traditional deferred annuities to plans, such as cash balance plans, that define benefits in terms of a current lump sum value that grows steadily over time in a fair and equitable manner. This shift in plan design has been occurring for good reason. Traditional plans provide benefits that are heavily backloaded economically and therefore deliver the bulk of their pension dollars to employees who spend all or most of their career with the sponsoring employer. The benefits these employees receive under most

traditional plans far outstrip their relative pay and service with the employer.

In most segments of the economy, the vast majority of employees do not spend anywhere near an entire career with a single employer and therefore miss out on the opportunity to earn meaningful retirement benefits even though they nominally are covered under a traditional defined benefit plan.[3] The benefits these employees receive under a traditional plan are insignificant in comparison to the benefits paid to long-service employees.[4]

The profiles of employees who fail to benefit under traditional defined benefit plans are as varied as the American workforce itself. Employees who change jobs at younger ages or in mid-career, for example, leave the employer when the value of traditional deferred annuities is de minimis at best. Conversely, employees who are hired in mid-career often arrive too late to build up substantial service under a traditional plan's benefit formula or to qualify for lucrative early retirement subsidies. For similar reasons, employees who interrupt their careers to raise a family or to care for an ailing relative often find the hiatus in employment has deprived them of crucial

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[3] *See* Letter from Senator Charles Grassley, Chairman U.S. Special Senate Committee on Aging, to David Walker, Comptroller General of the United States, U.S. General Accounting Office ¶ 5 (Aug. 4, 2000), *reprinted in* 2000 TNT 192-15 (Oct. 3, 2000) ("While [traditional defined benefit plans] tend to be very generous for those few employees that work for one employer their entire career . . . it is less beneficial when employees work for more than one employer during their working lives (the situation for the vast majority of all U.S. workers)."); GOVERNMENT ACCOUNTING OFFICE, CASH BALANCE PLANS: IMPLICATIONS FOR RETIREMENT INCOME, Report to the Chairman, Sen. Special Comm. on Aging (hereinafter the "GAO, CASH BALANCE PLANS"), GAO/HEHS-00-207, at 29 n.23 (Sept. 2000) ("median number of years any employee had with one employer was 4.7 years").

[4] In industries with low employee turnover, a traditional defined benefit plan can provide meaningful retirement benefits to most employees because most employees will fit the long-service career pattern needed to benefit from traditional deferred annuities. Even in industries with higher levels of employee turnover, a traditional plan can provide an effective means of rewarding long-service employees if that is the employer's principal retirement objective.

service credits needed to earn a meaningful benefit under a traditional plan, even if they return to work with the same employer. Because the value of traditional annuities declines after retirement age in most traditional plans, employees who are hired or continue to work after retirement age earn benefits that progressively decline in value as the older worker ages on the job.[5] The cumulative result of these individual experiences is an allocation of pension benefits across an employer's workforce that leaves large gaps in pension coverage for many employees.

The shortcomings of traditional defined benefit plans are not limited to the relatively small amount of benefits they deliver to most employees. The basic nature of traditional deferred annuity benefits is of concern as well. Most employees today want to know how much their retirement benefits are worth and want control over their retirement assets after they terminate employment. Traditional plans can pay out benefits in a single lump sum distribution that reflects the value of the employee's benefits and that can be rolled over into another retirement plan or an individual retirement account under the employee's control. However, the basic promise and only dollar guarantee of a traditional defined benefit plan is to pay out a deferred annuity. Because the value of the promised annuity fluctuates over time in response to interest rates, the amount of the lump sum distribution under a traditional plan is never guaranteed and instead is constantly at risk to changes in interest rates.

Cash balance plans address the shortcomings of traditional defined benefit plans by providing a more equitable distribution of benefits among employees and a stable cash balance account that precisely tracks the value of the employee's retirement benefit and is payable in a single lump sum distribution after termination of employment. Benefit accruals in a cash balance plan are spread out more evenly over an employee's career, in contrast to the backloaded

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[5] Forman, *Public Pensions: Choosing Between Defined Benefit and Defined Contribution Plans*, 1999 Det. C.L. Rev. 198-99; Council for Economic Development, *New Opportunities for Older Workers*, at 24-25 (1999), *available at* http://www.ced.org/docs/older.pdf.

benefit accruals in a traditional plan. As a result, all employees have the opportunity to earn meaningful retirement benefits regardless of their relative tenure with the sponsoring employer. Studies show that most employees receive significantly more valuable benefits under a cash balance plan than under a traditional defined benefit plan.[6]

Employers have achieved these laudable objectives by defining benefits in cash balance plans in a way that differs markedly from a traditional plan. As a technical matter, a "cash balance plan" is a defined benefit pension plan that determines an employee's benefit by reference to a hypothetical account balance, often referred to as the employee's "cash balance." An employee's accrued benefit at any point in time equals the balance in the hypothetical account at that time. Typically, the account balance grows each year by credits equal to a percentage of the employee's pay for the year (so-called "pay credits") and by credits in the nature of interest on the employee's account balance ("interest credits"). Generally, pay credits continue until the employee terminates employment with the sponsoring employer, while interest credits continue until the employee begins receiving benefits under the plan (even if benefits begin long after the employee has terminated employment with the sponsoring employer). In the typical cash balance plan, a participant is entitled to receive the account balance in a single lump sum distribution payable at any time after the participant terminates employment with the sponsoring employer. Alternatively, the participant can receive his or her benefit in the form of an annuity equal to the actuarial equivalent of the account balance at the time annuity payments begin.

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[6] *See, e.g.*, Watson Wyatt Worldwide, *The Unfolding of a Predictable Surprise: A Comprehensive Analysis of the Shift from Traditional Pensions to Hybrid Plans*, at iii (2000), *available at* http://www.watsonwyatt.com/homepage/us/res/cash_balance.htm; Kopp & Sher, *A Benefit Value Comparison of a Cash Balance Plan with a Traditional Final Average Pay Defined Benefit Plan*, Society of Actuaries Monograph (1998), *available at* http://www.soa.org/library/sectionnews/pension/PFN9810.pdf; *cf.* GAO, CASH BALANCE PLANS at 26, 29 n.23 ("[W]orkers employed by more than one employer during their career can receive more retirement income under multiple cash balance plans than multiple traditional defined benefit plans.").

B. The Decision of the Eleventh Circuit Fundamentally Alters the Benefits Payable under a Cash Balance Plan Based on an Interpretation of ERISA That Cannot Be Squared with the Statute.

As described above, an essential feature of cash balance plans is their ability to express an employee's benefit as a current lump sum value and to pay out that benefit in a lump sum distribution equal to the employee's current cash balance account. Without this feature, cash balance plans cannot achieve their objectives of distributing benefits equitably among employees and insulating the value of employees' benefits from changes in interest rates.

The Eleventh Circuit held in the case below that a lump sum distribution from a cash balance plan cannot be limited to an employee's cash balance account and instead must include an additional benefit. Under the methodology adopted by the Eleventh Circuit, commonly referred to as the "whipsaw" method, an employee's cash balance account must be projected forward to normal retirement age at the interest credit rate set forth in the plan and then discounted back to an actuarial present value using the statutory interest rates specified in ERISA section 203(e) and Code section 411(a)(11).[7] If the resulting amount exceeds the employee's current cash balance account, then the lump sum distribution payable to the employee must be increased to equal the amount so determined.

The Eleventh Circuit recognized that the additional benefit it was mandating would be payable any time the plan's interest credit rate exceeds the statutory interest rate. Projecting out an employee's cash balance account at the plan's interest credit rate and then discounting it back at a lower statutory interest rate will always yield an amount larger than the employee's cash balance account. The court also recognized that the amount of the additional benefit will increase the younger an employee is at the time he or she receives a

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[7] The precise steps for making this calculation are not entirely clear from the court's opinion.

lump sum distribution. This difference in amount based on the employee's age is attributable to the fact that the difference in interest rates which produces the additional benefit will apply over a longer period of time for younger employees and therefore will produce a larger additional benefit for them than for older employees. Indeed, if the court's method is applied strictly, in most cases the additional benefit will disappear entirely for any employee at or over normal retirement age at the time of distribution.

The Eleventh Circuit's interpretation of ERISA section 203(e) cannot be squared with the language of the statute. First, the whipsaw method appears nowhere in the statute or the implementing regulations. Instead, the method was inferred by the court from the general requirements of the statute and the language of the plan document in question. As far as the language of the plan document is concerned, the Eleventh Circuit simply got it wrong. Although the court insists that the plan document requires projecting forward an employee's cash balance account to normal retirement age at the plan's interest credit rate to determine the employee's accrued normal retirement age annuity, the plan says no such thing. On the contrary, the plan document is clear that, if an employee wishes to receive an annuity beginning at normal retirement age, the employee must wait until normal retirement age to see how large his or her cash balance account is at that point and therefore how much of an annuity he is entitled to receive under the plan's annuity conversion factors. Because the plan's interest credit rate is based on a variable index (as are most cash balance plans'), it is impossible to know in advance the size of the intervening interest credits and therefore the ultimate size of the account at any point in the future.[8]

Second, a statute must be interpreted in a manner that harmonizes all of its provisions. *See FDA v. Brown & Williamson Tobacco*

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[8] For this reason, the approach of projecting interest credits based on a variable index forward to normal retirement age is inherently problematic. *See Eaton v. Onan Corp.*, 117 F. Supp.2d 812, 833 (S.D. Ind. 2000); Pension Benefit Guaranty Corp., *Title IV Aspects of Cash Balance Plans with Variable Indices*, 65 Fed. Reg. 41610, 41611-12 (July 6, 2000).

Corp., 529 U.S. 120, 133 (2000) ("A court must . . . interpret [a] statute as a symmetrical and coherent regulatory scheme, and fit, if possible, all parts into an harmonious whole.") (internal quotations and citations omitted); *Richards v. United States*, 369 U.S. 1, 11 (1962) ("We believe it fundamental that a section of a statute should not be read in isolation from the context of the whole Act."). An interpretation that places two provisions of the same statute in conflict with one another is to be disfavored over an alternative interpretation that does not. *United States v. Moore*, 95 U.S. (5 Otto) 760, 762-63 (1877) (rejecting an interpretation of one statutory provision which would conflict with another); *United States v. Shewmaker*, 936 F.2d 1124, 1128 (10th Cir. 1991). The additional benefit mandated by the Eleventh Circuit's whipsaw method produces large disparities in benefits among employees based solely on their relative ages. Employees of different ages who have the same pay and service history with the employer (and therefore the same size cash balance accounts) will receive dramatically different lump sum benefits based solely on the difference in their ages. A younger employee will receive a larger lump sum than a middle-aged employee who, in turn, will receive a larger lump sum than an employee past normal retirement age, who in most cases will derive no benefit from the whipsaw calculation at all. This disparate treatment of older employees under ERISA section 203(e) is difficult to reconcile with ERISA section 204(b)(1)(G) and (H), which generally bars such age-specific effects in defined benefit plans.

Third, the whipsaw method not only is not required by ERISA section 203(e), it actually violates it. An employee who terminates employment before normal retirement age faces a dilemma under the Eleventh Circuit's opinion. If the employee does not consent to an immediate lump sum distribution and instead leaves his or her benefit in the plan until normal retirement age, the employee will forgo entirely the additional benefit mandated by the Eleventh Circuit. For younger employees especially, the amount of additional benefit lost could be substantial. However, the implementing Treasury regulations under ERISA section 203(e) and the parallel Code section 411(a)(11) specifically prohibit a plan from imposing a substantial detriment on any employee who does not consent to an

immediate distribution. *See* Treas. Reg. § 1.411(a)-11(c)(2)(i). The Internal Revenue Service has found a substantial detriment to exist as a result of plan provisions and practices with far less economic significance than that at stake here. *See* Rev. Rul. 96-47, 1996-2 CB 35. It is apparent that the Eleventh Circuit cannot reasonably interpret section 203(e) to require a plan to violate that same section.

Fourth, the Eleventh Circuit apparently requires a cash balance plan to convert an employee's current account balance into a deferred annuity beginning at normal retirement age by projecting forward the account balance at the plan's interest credit rate. This method is directly at odds with the provisions of the statute that govern how an accrued benefit expressed in the form of an annuity beginning at normal retirement age is to be derived for a plan that does not define its benefits in that way.[9] The present value requirements of ERISA section 203(e) and Code section 411(a)(11) apply to an employee's nonforfeitable "accrued benefit." ERISA section 3(23) and Code section 411(a)(7)(A)(i) define the term "accrued benefit" for this purpose. The implementing regulation under those sections, Treas. Reg. § 1.411(a)-7(a)(1)(ii), provides that in the case of a defined benefit plan that does not provide an accrued benefit in the form of an annuity beginning at normal retirement age, the term "accrued benefit" means an annuity beginning at normal retirement age that is the "actuarial equivalent (determined under section 411(c)(3) . . .) of the accrued benefit determined under the plan." Internal Revenue Service guidance under Code section 411(c)(3) in turn provides that actuarial equivalence for this purpose is to be determined using the interest rate assumptions of Code section 417(e), not the interest credit rate set forth in the plan. *See* Treas. Reg. § 1.411(c)-1(e)(1); IRS Announcement 95-33, ¶ 362.1(1)(a), 1995-19 I.R.B. 14.

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[9] The Eleventh Circuit in the decision below observed that the plan in this case defines the accrued benefit in terms of an annuity commencing at normal retirement age. However, the definition cited by the court is not part of the operative provisions of the plan and is set forth only for the limited purposes illustrated above at page 5. The operative provisions of the plan make clear that the benefit promised employees is an immediate lump sum distribution in the amount of the participant's current cash balance account.

Applying the method specified in the statute leads to entirely different results from the whipsaw method embraced by the Eleventh Circuit. The method specified in the statute requires a plan to convert an employee's current account balance into an actuarially equivalent annuity beginning at normal retirement age using the interest rate assumptions of Code section 417(e). Discounting this actuarially equivalent annuity back to present value using the same interest rate assumptions (which also apply under ERISA section 203(e) and Code section 411(a)(11)) yields a minimum lump sum distribution that exactly equals the employee's cash balance account.

II. THE COURT SHOULD ADDRESS THE PROPER DEGREE OF DEFERENCE TO BE ACCORDED BY THE COURTS TO IRS DETERMINATION LETTERS.

This case also presents the Court with the opportunity to consider the propriety of the Eleventh Circuit's failure to accord any deference to the determination letter issued by the Internal Revenue Service (the "IRS") approving the Georgia-Pacific Plan. The Eleventh Circuit concluded that, although the IRS reviews determination letters with a checklist that includes compliance with Code section 417(e),[10] and despite the absence of any other applicable regulatory guidance, the determination letter issued by the IRS is not to be accorded any weight.[11]

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[10] *See* Worksheet Number 2A—Determination of Qualification (Department of Treasury – Internal Revenue Service) 2000, at V.g. (Appendix 77a to Petitioners' Petition for a Writ of Certiorari).

[11] The Eleventh Circuit noted that, remarkably, the IRS urged the court not to consider the determination letter that it issued. This Court has recognized that an agency's litigation position may not reflect an agency's considered judgment on an issue because litigation counsel does not make policy for an agency. *See, e.g., Bowen v. Georgetown Univ. Hosp.*, 488 U.S. 204, 212 (1988). In this case, the IRS's litigating position does not appear to have been accepted by policy-making officials at the IRS given that there has been no attempt by the IRS to revoke the large numbers of favorable determination letters it has issued to cash balance plans that do not apply the whipsaw approach.

This Court has repeatedly stated that ERISA is an "enormously complex and detailed" statute, *Mertens v. Hewitt Assocs.*, 508 U.S. 248, 262 (1993), compliance with which requires constant attention and judgment from employers, plan administrators, and their advisors. In recognition of this fact, Congress has established a process by which plan sponsors may obtain certainty—before voluntarily undertaking the multi-million dollar obligation to provide retirement benefits—that the form of its retirement plan satisfies the requirements of the Internal Revenue Code. In this process, the IRS accepts comments submitted by interested employees and reviews a retirement plan's form for compliance with the qualification requirements of the Code. Frequently, this process includes discussions between the IRS and a plan sponsor, and sponsors often amend plans in response to the IRS's comments. Once the IRS is satisfied that a plan meets the qualification requirements of the Code, it issues a determination letter stating only the conclusion that the form of the plan is qualified under the Code.

Absent the determination letter process, the risk associated with adopting a retirement plan would increase dramatically and employers would likely be dissuaded from adopting retirement plans. This is especially true when employers confront areas of the law for which no guidance of general applicability exists. In such cases—for example, with respect to cash balance plans—employers have only determination letters on which to rely. In such situations, consulting firms such as amici may rely on a series of such letters issued to plans that they have designed. Should determination letters carry no weight in court, the process set forth to provide plan sponsors with certainty will not achieve its purpose.

Deference should also be given to determination letters to ensure that retirement plan sponsors and fiduciaries are subject to a uniform regulatory scheme. ERISA was enacted to provide a single regulatory regime to govern employee benefit plans. *Cf. New York State Conference of Blue Cross & Blue Shield Plans v. Travelers Ins. Co.*, 514 U.S. 645, 657 (1995) ("The basic thrust of [ERISA's] preemption clause, then, was to avoid a multiplicity of regulation in order to permit the nationally uniform administration of employee benefit

plans."). Accordingly, Congress has sought in many instances to limit interpretive authority over parallel provisions in the Code and ERISA to one agency. *See, e.g.*, ERISA § 3002(c), 29 U.S.C. § 1202(c) (Treasury regulations under Code sections 410(a), 411, and 412 apply to the parallel provisions in ERISA). If courts accord no weight to determination letters, plan sponsors and fiduciaries may confront conflicting regulatory requirements imposed by identical statutory provisions. This is, in fact, the result reached by the Eleventh Circuit in the case below. *See*, Part I, *supra*.

CONCLUSION

Amici respectfully ask the Court to grant certiorari in this case to preserve the broad authority accorded employers in determining how to provide retirement benefits to their employees and to provide the lower courts with greater direction as to their ability to second-guess the administrative guidance on which employers and plan administrators must, by necessity, rely.

The petition for certiorari should be granted.

Respectfully submitted,

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IN THE

Supreme Court of the United States

GEORGIA-PACIFIC CORPORATION SALARIED EMPLOYEES RETIREMENT PLAN AND GEORGIA-PACIFIC CORPORATION,

Petitioners,

v.

JERRY L. LYONS, individually and on behalf of all other persons similarly situated,

Respondents.

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE ELEVENTH CIRCUIT

MOTION FOR LEAVE TO FILE BRIEF AMICI CURIAE AND BRIEF AMICI CURIAE OF THE NATIONAL ASSOCIATION OF MANUFACTURERS AND THE AMERICAN BENEFITS COUNCIL IN SUPPORT OF PETITIONERS

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MOTION OF AMICI CURIAE NATIONAL ASSOCIATION OF MANUFACTURERS AND AMERICAN BENEFITS COUNCIL FOR LEAVE TO FILE BRIEF AMICI CURIAE IN SUPPORT OF PETITIONERS

Pursuant to Supreme Court Rule 37.2, the National Association of Manufacturers ("NAM") and the American Benefits Council (the "Council") hereby move this Court for an order granting leave to file the accompanying Brief Amici Curiae in support of Petitioners. The consent of counsel for Respondent Jerry L. Lyons was requested and refused, necessitating this motion.

The interest of amici curiae arises from the uncertain, unanticipated, and potentially uncabined liability faced by their members' employer-sponsored cash balance pension plans as a result of the Eleventh Circuit's decision in this case. Amici curiae believe the decision may undermine the financial stability of existing cash balance pension plans and leave plan sponsors with no guidance on how properly to value future voluntary lump sum distributions to plan participants.

Amicus curiae NAM is the nation's largest and oldest multi-industry trade association. The NAM represents 14,000 member companies (including more than 10,000 small and mid-sized manufacturers) and 350 member associations serving manufacturers and employees in every industrial sector and all 50 states. Over 158,000 additional businesses are affiliated with the NAM through its National Industrial Council and its Associations Council.

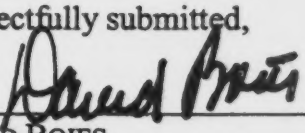
Amicus curiae the Council (formerly the Association of Private Pension and Welfare Plans) is a broad-based, non-profit trade association founded in 1967 to protect and foster the growth of the private employer-sponsored employee benefit plan system in the United States. The members of the

Council include small and large employer sponsors (including many Fortune 500 companies) of employee benefit plans, as well as numerous plan support organizations such as consulting and actuarial firms, investment firms, banks, insurers, and other professional benefit organizations. Collectively, the Council's members sponsor or administer plans covering more than 100 million participants.

Both the NAM and the Council have filed briefs amicus curiae before this Court and other courts in numerous cases involving important employee benefit plan issues and have frequently testified before Congress regarding such issues.

Because of the breadth and significance of the issues arising out of the Eleventh Circuit decision, the NAM and the Council respectfully request leave to file their Brief Amici Curiae.

Respectfully submitted,



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March 2, 2001

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IDENTITY AND STATEMENT OF INTEREST OF AMICI CURIAE[1]

Amici curiae NAM and the Council are nationally based trade associations whose members include thousands of employers and employer-sponsored employee benefit plans and numerous plan support organizations. The NAM represents 14,000 member companies (including more than 10,000 small and mid-sized manufacturers) and 350 member associations serving manufacturers and employees in every industrial sector and all 50 states. Collectively, members of the Council sponsor, administer or support health, retirement, and other benefit plans covering more than 100 million participants.

The NAM and the Council's interest here arises from the uncertain, unanticipated, and potentially uncabined liability faced by their members' employer-sponsored cash balance pension plans as a result of the Eleventh Circuit's decision in this case. Amici curiae are concerned that the decision will undermine the financial stability of existing cash balance pension plans and leave plan sponsors with no guidance on how properly to value voluntary lump sum distributions to plan participants.

SUMMARY OF ARGUMENT

Employer-sponsored retirement plans play a critical role in providing income security to the American workforce, providing retirement income for more than 91 million employees. In that role, these plans have been enormously successful. Trillions of dollars are invested in the employer-sponsored retirement benefit system, which pays more than

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[1] Counsel for amici curiae NAM and the Council authored this brief in its entirety. No person or entity, other than the amici, their members, or their counsel, made a monetary contribution to the preparation or submission of this brief.

$240 billion in private sector employee retirement benefits each year. The cash balance plans at issue in this case are a relatively new, innovative form of employer-sponsored defined benefit plan that address many of the particularized needs of the modern, increasingly mobile workforce and are now used by approximately twenty percent of Fortune 1000 companies.

Employers, however, will only invest the trillions of dollars required to fund employee retirement plans if they can have certainty in their future obligations, including certainty and clarity of the amount that the employee is entitled to, and the amount for which the plan is liable, at the time of employee/employer separation. If employers cannot rely on the plain meaning of statutes or even on applicable federal agency interpretations made in individual determination letters, the effectiveness of the private-employer pension system is fatally undermined. Employers must have reasonable certainty in order to innovate and compete. For years, plan sponsors established and funded cash balance pension plans in reliance on ERISA §203(e), 29 U.S.C. §1053(e)'s plain language limiting its application to involuntary distributions. Plan sponsors maintained those plans in reliance on specific, individualized determinations by the IRS that the plans complied with all applicable regulations, including those that govern the valuation of lump sum distributions.

That reliance, and the settled expectations that rest on it, were abruptly upended by the Eleventh Circuit's decision in *Lyons v. Georgia-Pacific Corp. Salaried Employees Retirement Plan*, 221 F.3d 1235 (11th Cir. 2000). By holding that the present value of a lump sum cash distribution had to be determined by projecting an employee's current retirement account balance forward to retirement age using the plan's crediting rate, and then discounting that projected balance back to a present value using a different rate specified by

I.R.C. §417(e), regardless of whether the crediting rate was at a historical peak or trough at the time of separation, the *Lyons* decision created a new "project forward" requirement that upended a previously settled, ordered world.

The decision contradicts the plain meaning of ERISA §203(e) by interpreting that provision to require current cash balances to be projected forward. The decision effectively imposes, retroactively, an interpretation of ERISA §203(e) found only in proposed IRS regulations that have never been finally promulgated, and that by their own terms were intended to have only prospective effect once promulgated. The decision provides plan sponsors with no guidance as to how the Eleventh Circuit's untested new rule should be applied. Finally, the decision effectively turns the one safe harbor for plan sponsors under existing laws into a trap, since plans that seek the shelter of this safe harbor of the tax laws (applying provisions that are substantively identical to ERISA §203(e)) will, as a practical matter, almost always face liability to plan participants under the *Lyons* court's interpretation of ERISA §203(e).

This disruption of settled expectations, combined with the prospect of continuing instability and uncertain liability, can only serve to discourage the development and maintenance of vitally important private employer pension plans, and thus necessitates review by this Court.

ARGUMENT

I. THE ELEVENTH CIRCUIT'S DECISION UPSETS SETTLED EXPECTATIONS OF CASH BALANCE PLAN SPONSORS.

The Eleventh Circuit's decision is wholly inconsistent with the settled expectations of cash balance plan sponsors and retroactively imposes hundreds of millions of dollars in pension obligations that plan sponsors never funded, plan

participants never anticipated, and the law never before required.

Prior to the *Lyons* decision, several principles for cash balance plans were clear.

First, by establishing a bookkeeping account that expresses as a single sum the value of an employee's retirement benefit at any given time, cash balance plans improved participants' understanding of the value of their retirement benefits, a feature previously lacking in traditional defined benefit pension plans. *See* GOVERNMENT ACCOUNTING OFFICE, CASH BALANCE PLANS: IMPLICATIONS FOR RETIREMENT INCOME, Report to the Chairman, Sen. Special Comm. on Aging (hereinafter the "GAO, CASH BALANCE PLANS"), GAO/HEHS-00-207, at 19 (2000).

Second, cash balance plans routinely provided that plan participants who elected a lump sum distribution upon separation from their plan would receive the actual value of their bookkeeping accounts at the time of separation.

Third, the IRS, in determination letters provided to employers with cash balance plans structured in exactly this way, had expressly and repeatedly "determine[d] that the[se] plan[s] fully complied with all applicable regulations." *See* Pet. App. 86a. This determination necessarily included a verification of compliance with the rules in I.R.C. §417(e) regarding the valuation of elective lump sum payments. *See* Treas. Reg. §601.201(a)(3); IRS Worksheet Number 2A – Determination of Qualification (Department of the Treasury – Internal Revenue Service) 2000, at V.g. (Pet. App. 77a).

Fourth, neither ERISA, nor the Internal Revenue Code, nor any other statute or regulation provided any guidance as to how the present value calculations contained in ERISA §203(e) might apply to the unique issues raised by voluntary distributions under cash balance plans. *See, e.g.,* Title IV Aspects of Cash Balance Plans with Variable Indices, 65 Fed.

Reg. 41610, 41611-12 (July 6, 2000) (soliciting public comments, in context of plan termination under ERISA Title IV, regarding what method to use to value lump sum payments under cash balance plans and analyzing pros and cons of possible approaches). In particular, nothing in ERISA §203(e) or Treasury Regulation §1.411(a) sets forth, or even suggests, a "project forward" methodology for valuing voluntary lump sum distributions. Indeed, on its face, ERISA §203(e) has nothing whatsoever to do with voluntary, as opposed to mandatory distributions, and the discounting methodology set forth in this provision is only "For purposes of" making determinations under "paragraph 1" regarding whether a lump sum distribution can be made "without the consent of the participant."

Fifth, the first suggestion anywhere that a "project forward" methodology might be appropriate in certain circumstances appears in the preamble to a regulation under I.R.C. §401(a)(4). *See* 56 Fed. Reg. 47524, 47528. The infirmity of this authority, however, is revealed by the fact that the IRS itself continued to issue determination letters approving cash balance plans that did not include "project forward" provisions even after the date of the proposed regulations – a clear recognition by the IRS that the calculation methodology in the §401(a)(4) regulations was not universally applicable.

Finally, the only time the IRS made even a tentative attempt to define or apply a "project forward" methodology to value lump sum distributions in cash balance plans was in IRS Notice 96-8, issued in 1996. *See* I.R.S. Notice 96-8, 1996-1 C.B. 359. This Notice, however, only reinforced the view that no such methodology was required under existing law, stating in its "Purpose" section: "The proposed guidance is being described in this notice in order to permit advance public comment in anticipation of regulations that incorporate the proposed guidance." (To date, this "proposed

guidance" has still not been finalized.) The Notice also included a safe harbor provision "for plan years beginning before regulations are effective" that saved plans from tax disqualification where they had made distributions based on a "reasonable, good-faith interpretation of the applicable provisions of the Code, taking into account preexisting guidance."

Acting in this legal environment, plan sponsors established, administered, and funded cash balance plans with the settled expectations that compliance with ERISA and the tax laws required nothing more than to pay plan participants voluntary lump sum distributions that were exactly equal to what had been promised in plan documentation and what the participants themselves expected, *i.e.*, the amount in their bookkeeping accounts. IRS Notice 96-8 was the first time any new methodology was even suggested, and, even then, the IRS recognized that the "project forward" methodology was a change in the law that was simply being explored on a prospective basis with accommodation to be made for the fact that employers had never understood this approach to be legally required.[2]

By turning this settled universe on its head, the Eleventh Circuit's decision not only potentially imposes hundreds of millions of dollars of unexpected and unfunded obligations (which ultimately must be guaranteed by the Federal Government through the Pension Benefit Guaranty Corporation, *see, e.g.*, *Pension Benefit Guar. Corp. v. LTV Corp.*, 496 U.S. 633, 637-38, 110 S. Ct. 2668, 2671 (1990)), but also creates a climate of uncertainty that will have a

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[2] Significantly, even after issuing Notice 96-8, the IRS has never made any attempt to tax disqualify cash balance plans that had received favorable determination letters. Nor has the IRS ever invoked the formal procedure for revoking those determination letters, *see* 26 C.F.R. 601.201(l)(4)-(5).

chilling effect on the development and maintenance of private employer pension plans across the U.S. economy.

Private employer pension plans are critical to the retirement income of American workers. Such plans pay almost one third of pension income received by retirees in the United States, and the employer-sponsored retirement system in the U.S. pays more to retirees than does Social Security. *See* "Finances of Employee Benefits", EBRI NOTES (July 2000). Cash balance plans, in particular, have become an increasingly popular form of pension plan for employers who recognize that traditional plans heavily backload benefit accrual, thereby disadvantaging younger, lower-paid, and more mobile employees, as well as those who leave and return to the workforce, or who wish to work beyond retirement age. See Richard C. Shea, et al., *Age Discrimination in Cash Balance Plans: Another View*, 19 VA. TAX. REV. 763, 764-65 (2000). Because cash balance plans address these shortcomings they have been adopted in recent years by one in five Fortune 1000 companies, which find them an effective recruiting tool. See GAO, CASH BALANCE PLANS at 17-18, 42.

The decision to establish or continue a private pension plan is, however, purely voluntary. Employers' willingness to contribute many billions of dollars in their voluntary retirement plans or to adopt innovative pension plan solutions (like cash balance plans) depends on the availability of some advance certainty regarding the legality of their plans, and the exact obligations plan sponsors will be assuming. *See, e.g.*, GAO, CASH BALANCE PLANS, at 42 (continued uncertainty about cash balance plans discouraged plan sponsors from adopting them). Currently, the only mechanism for gaining advance certainty is the legal determination letters provided by the IRS. Indeed, "the favorable determination letter serves as an 'insurance policy' for the practitioner and the employer that the retirement plan is qualified as to form and,

in certain circumstances, as to operation." Barbara A. Breeding, *Qualifying a Plan Through the IRS*, SD81 A.L.I.-AB.A. 571, 573 (1999). *See also* Kenni B. Merritt, *Voluntary Governmental Compliance Programs: Chicken Soup for the Employee Benefit Plan*, 25 Okla. City U. L. Rev. 351, 357 (2000) (to same effect). Accordingly, "employers routinely have sought and obtained the blessing of the IRS on the qualification of their cash balance conversions." Unifi Network, *A Unifi Survey of Conversions from Traditional Pension Plans to Cash Balance Plans* [hereinafter, *Unifi Survey*], at 16 (2000). *See also id.* at 15-16 & t.5 (reporting that 55 of 57 surveyed firms that converted to cash balance plans between 1985 and 1996 had obtained favorable determination letters). Whatever weight such letters carry outside of the tax qualification of pension plans, as a practical matter employers must be able to place some reliance in the representations of the federal agency charged with administration of the very statute in question.

Yet, by ignoring settled expectations that were well-founded in the language of the ERISA statute, the Treasury Regulations, and in the IRS's own determination letters, the Eleventh Circuit's decision creates an environment that can only work to discourage plan sponsors' overall willingness to provide pensions to their employees. Indeed, after the *Lyons* decision, adoption of any innovative new pension plan is a fool's game, since the ultimate funding obligation for such a plan is completely indeterminate, regardless of what the IRS might say. For these reasons, the Eleventh Circuit's decision raises questions of particular importance for plan sponsors nationwide and indeed, for the retirement security of American workers.

II. THE DECISION BELOW IMPOSES AN UN-ADMINISTRABLE OBLIGATION ON PLAN SPONSORS WHILE CREATING AN IRRECONCILABLE CONFLICT BETWEEN SUBSTANTIVELY IDENTICAL ERISA AND IRS RULES.

The Eleventh Circuit's decision not only retroactively upsets settled expectations, but, even *prospectively*, sets plan sponsors adrift, without any guidance on how to apply the "project forward" calculation the Eleventh Circuit finds in ERISA §203. This uncertainty is all the more significant in light of the IRS's contrary interpretation of its substantively identical rules.

The Eleventh Circuit held that payment of a voluntary lump sum benefit prior to retirement requires that a cash balance plan project the employee's existing bookkeeping account balance *forward* to retirement age using the plan's interest crediting rate, and then discount the value of the benefit *back* to the present using a different interest rate in I.R.C. §417(e). 21 F.3d at 1251. The Eleventh Circuit's decision, however, fails to recognize that its creation of a "project forward" requirement for cash balance plans leaves wholly unanswered the question of how a "project forward" methodology should apply. There is no clear answer to this question because any "project forward" requirement must make an inherently speculative assumption about a variable index's future performance after the date the lump sum distribution is paid.[3]

Indeed, the Pension Benefit Guaranty Corporation ("PBGC") is still struggling with this question. In the context of a recent request for public comments regarding the

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[3] Although a fixed crediting rate avoids this particular issue, the great majority of cash balance plans base interest credits on variable indices like the Treasury bond rates. *See* note 3, *infra*.

valuation of cash balance plans upon plan termination, the PBGC noted several possible approaches: designating a standardized value that would apply to all plans that terminated on a given date; making a "best estimate" determination for each plan termination; using the index as it stood on the plan's termination date (the "spot rate"); or using some "historical average" of the index. *See* 65 Fed. Reg. at 41612.

The PBGC recognized, however, that each of these approaches has its downsides: "a standardized PBGC value could lead to results that would diverge significantly from what one would expect based on the variable index a plan chose"; the "'best estimate' approach might leave too much discretion with the PBGC"; the "spot rate" approach raises issues "where the index was at (or near) a historic high or low or where, as in the case of an equity index, the change in the index could be negative"; and "the 'historical average' approach would raise questions as to the period over which the variable index should be averaged . . ., the method of averaging, [and] the data's applicability to the future, particularly where the variable index had existed only for a short time or was volatile (*e.g.*, a stock index)." *Id.* Ultimately, the PBGC said it was "actively considering" an approach that "combine[d] elements of the "spot rate" and "historical average." *Id.*

Instead of recognizing the nuances of this problem, the Eleventh Circuit's decision exacerbates it by assuming the issue away. The Eleventh Circuit effectively determined that Georgia-Pacific should use the spot rate to project forward Lyons' retirement benefits. But, the Eleventh Circuit's reasoning was wholly predicated on an erroneous presumption that the "Plan itself" specifies that Respondent's "hypothetical account balance must be projected forward using" what was the spot rate. *Lyons*, 221 F.3d at 1252.

Thus, the Eleventh Circuit's decision opens a void for plan sponsors nationwide by simply referring back to the "Plan itself", which, in many cases (including Georgia-Pacific's Plan, contrary to the Eleventh Circuit's determination), does not identify an appropriate crediting rate – be it the "historical rate," the "spot rate" the "best estimate rate," or some blend of some or all of the above – because, at the time the plans were created, no one contemplated a "project forward" requirement. This creates an untenable situation for plan sponsors who, under the Eleventh Circuit's rule, are subject to liability for failing to project forward, but are offered no guidance on what methodology they can use to insulate themselves from liability.

Nor are plan sponsors assisted by assuming that the Eleventh Circuit is requiring an across-the-board application of the spot rate (*i.e.*, the prior year's crediting rate) for the project forward calculation, something the Eleventh Circuit actually did not hold. As the PBGC recognized, using the spot rate can lead to wild and unpredictable swings in plan sponsors' liabilities and employees' accounts, particularly where a volatile stock index forms the basis of the crediting rate and the "index was at (or near) a historic high or low or where, as in the case of an equity index, the change in the index could be negative." 65 Fed. Reg. at 41612.[4]

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[4] The Eleventh Circuit dismissed the stock index issue as a "farfetched" "hypothetical." 221 F.3d at 1249 n.23. In fact, as the PBGC comments show, it is a very real issue. Indeed, a recent survey of 100 cash balance plans identified two plans that used variable interest crediting rates based on mutual fund index returns. *See Unifi Survey*, at 49-51. Regardless, even a crediting rate based on a 10-year Treasury security can vary significantly over the course of a few years, variations that, when compounded forward to retirement age, will themselves create great disparities and huge administration problems for plan sponsors applying the Eleventh Circuit's rule. For example, the yield on 10-year Treasury Constant Maturities (one of the safe harbors designated in Notice 96-8) fluctuated between 7.42 percent in 1977 and 13.92 percent in 1981, and

Not only does the Eleventh Circuit's decision create a void for plan sponsors, it also simultaneously removes the sole existing guidance on this difficult issue. IRS Notice 96-8 tentatively suggests a prospective "project forward" requirement like the one the Eleventh Circuit imposed.[5] The IRS, however, plainly recognized (in a way that the Eleventh Circuit did not) that there can be no computational certainty in "projecting forward" benefits to retirement age. Thus, the IRS provided for a number of "safe harbor" interest crediting rates that plan sponsors could use and thereby *avoid* the "project forward" requirement altogether yet still be certified as "tax qualified." These "safe harbor rates" attain a rough equivalence with the discount rate in I.R.C. §417(e) (30-year Treasury bonds) such that dispensing with the project forward/discount back approach leads to roughly the same result as simply using the current balance in a participant's bookkeeping account.[6]

But, the Eleventh Circuit's decision – based on substantively identical provisions of ERISA – turns this safe harbor into a trap by creating a rule that almost invariably results in cash balance plans incurring liability to plan

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then fell back to 7.67 percent by 1986. *See* Federal Reserve Statistical Release H.15, Selected Interest Rates (Feb. 20, 2001).

[5] As discussed, Notice 96-8 does not, however, support the Eleventh Circuit's retrospective application of the "project forward" rule; indeed, its explicit language directs that the rule should apply only prospectively, *see* I.R.S. Notice 96-8, 1996-1 C.B. 359, at IV.B, and creates a safe harbor for plan sponsors who did not apply the project forward methodology before the regulations were promulgated, *see id.* at IV.A.

[6] In other words, projecting the existing balance forward using one rate and then discounting back using a different, but roughly similar rate, will lead to a result that approximates the existing account balance. Through its choices of acceptable safe harbor crediting rates (which are different from, but have historically been roughly equal to the 30-year Treasury bond rate used in I.R.C. §417) the IRS ensures this result.

participants whenever the safe harbor is used. This creates inconsistent obligations that effectively render the safe harbor provision of Notice 96-8 meaningless. While, for tax qualification purposes, a plan sponsor theoretically could adopt one of the safe harbor crediting rates to make voluntary lump sum distributions equal to the current value of a participant's bookkeeping account, no plan sponsor can realistically take advantage of this option since, under *Lyons*, the plan sponsor would still be subject to liability if it made this lump sum distribution.[7]

Plan sponsors who voluntarily choose to offer pension plans and then comply with all IRS rules should not be subjected to court-imposed liability to plan participants under the identically worded provisions of ERISA. This untenable situation is exactly what Congress has historically sought to prevent. *See generally* ERISA §3002(c), 29 U.S.C. §1202(c); Reorganization Plan No. 4 of 1978, §104, 92 Stat. at 3791 (in pursuing civil actions to enforce "Parts 2 and 3 of Subtitle B of Title I of ERISA...the Secretary of Labor shall be bound by the regulations, rulings, opinions, variances, and waivers

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[7] As Georgia Pacific has ably demonstrated in its own brief, this is not a hypothetical threat. *See* Petition for Writ of Certiorari, No. 00-1234, at 23-24. For example, Notice 96-8 allows cash balance sponsors to comply with ERISA §203(e) and Treasury Reg. §§1.411(a)-11 and 1.417(e)-1(d) by using a "safe harbor" interest crediting rate equal to the prevailing three-month Treasury bill rate plus 175 basis points (1.75%). Thus, under Notice 96-8, use of this crediting rate would permit a plan sponsor to distribute to a participant a lump sum equal to the current bookkeeping account balance even in months (as has historically been the case) when the gap between this crediting rate and the Code §417(e) discount rate has been as high as 100 basis points. Yet, under *Lyons*, a plan sponsor, even after complying with Notice 96-8 and receiving a favorable tax determination letter, would still be subject to liability under Title I of ERISA for making precisely this distribution. Indeed, the Eleventh Circuit imposed liability on Georgia-Pacific for failing to "project forward" where the gap between the crediting rate and the Code §417(e) discount rate was only 75 basis points.

issued by the Secretary of the Treasury"). Yet, the Eleventh Circuit simply dismissed the problem without concern for the fact that Georgia-Pacific could "be safely harbored only from tax disqualification, [but] not from liability to plan participants." 221 F.3d at 1250 n.28.

Broadly applied, this holding threatens to unravel the closely knit scheme for congruent tax and liability regulation of pension plans, with profound consequences for plan sponsors. Even narrowly applied, the holding effectively obliterates the safe harbor provisions of IRS Notice 96-8 and leaves plan sponsors at sea as to how they might apply a "project forward" methodology that would insulate them from liability under the Eleventh Circuit's new rule. For these reasons, the Eleventh Circuit's decision raises a question of exceptional importance for pension plan sponsors nationwide.

CONCLUSION

For the foregoing reasons, amici curiae respectfully submit that the petition for certiorari should be granted.

Respectfully submitted,

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